The CBSA Decision In Certain Laminate Flooring

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The Canada Border Services Agency ("CBSA") issued its Statement of Reasons in the *Certain Laminate Flooring* dumping and subsidy case on June 1, 2005.[1] The conduct of the investigation and the decision and reasons are significant in a number of respects. First, the CBSA has formally renounced the practice of "zeroing" in the calculation of dumping margins, thereby formally bringing Canada's practice in line with WTO requirements. Second, the CBSA permitted all parties to participate in the investigation process to a much greater extent than has been its previous practice. Third, the CBSA continued its practice in recent cases of treating China as a market economy and examined a number of subsidy programs in China. The conclusions set out in the Statement of Reasons provide useful guidance for importers of Chinese goods on how the CBSA will treat such programs in future countervailing duty cases.

Background

The complaint in *Certain Laminate Flooring* was initiated by Uniboard Surfaces Inc., the sole producer of laminate flooring in Canada. The complaint alleged that imports of laminate flooring from China, France, Austria, Belgium, Germany and Poland were being dumped and that the imports from China were also subsidized.

Dumping occurs if the "export price" of imported goods (i.e. the price for which they are sold for export to Canada) is lower than the "normal value" of the goods (i.e. the domestic price in the exporting country or their cost plus a reasonable amount for profit). If dumped imports cause injury to domestic producers of like goods, the importing country can impose an antidumping duty to offset the effect of the dumping.

Subsidies can take the form of grants, preferential loans, tax breaks and government provision of goods or services for inadequate remuneration. A subsidy must be specific to particular enterprises or industries in order to be "actionable". If subsidies received by producers or exporters are specific and the subsidized exports cause material injury to domestic producers of like goods in the importing country, the importing country can impose a countervailing duty to offset the effect of the subsidy. A subsidy that is not specific is not "actionable" and cannot be subject to a countervailing duty.

The CBSA determines whether imports are dumped or subsidized and the Canadian International Trade Tribunal determines whether the dumping or subsidization has caused injury. On May 17, 2005, the CBSA issued its final determination in *Certain Laminate Flooring*, in which it found that the imports of laminate flooring from China and France were dumped and the imports from China were also subsidized. The CBSA did not find that imports from the other countries had been either dumped or subsidized, and terminated its investigation respecting those imports.

The Tribunal, which commenced its injury inquiry in February, held an injury hearing immediately after the CBSA released its final determination. On June 16, 2005, the Tribunal released its decision that dumped imports from China and France and subsidized imports from China have materially injured the domestic industry, meaning that imports of laminate flooring from France and China will be subject to antidumping duties and imports from China will also be subject to countervailing duties.

[1] See http://www.cbsa-asfc.gc.ca/sima/anti-dumping/ad1332f-e.html

Renunciation Of Zeroing

Dumping calculations involve the comparison of normal values with export prices. If the export price (the price at which the goods are sold for export to the importing country) is less than the normal value of the goods (the price at or above which the goods should have been sold for export to the importing country), the margin of dumping (difference between the normal value and the export price) is positive and the goods are considered as "dumped." If, however, the export price exceeds the normal value, the margin of dumping is negative and the goods are undumped. Dumping calculations may involve multiple price comparisons. For example, there may be many different product models of the good under consideration, and a separate calculation of dumping margin can be made for each model. The dumping margins for some models may be positive while others may be negative. The practice of zeroing ignores all the negative margins and values them at zero before taking a weighted average of all the margins to arrive at an overall dumping margin for all the goods. Zeroing guarantees a positive margin of dumping unless the margins for all models are zero or negative.

Zeroing and the WTO

The predecessors of the CBSA (the Canada Customs Revenue Agency, or CCRA, and previously the Deputy Minister of National Revenue), like their counterparts in the United States and the European Union, all practiced zeroing in response to pressure from domestic industries desiring high dumping margins with consequent high antidumping duties to protect them from import competition.

Zeroing was brought under WTO scrutiny in a case brought by India against the European Union respecting bed linen.[2] The panel and the Appellate Body condemned the practice as not providing the fair comparison between normal values and export prices that the WTO Antidumping Agreement requires. The European Union complied with the ruling and has discontinued zeroing.

The Bed Linen decision left Canadian authorities with a dilemma. Canadian steel producers, who have made extensive use of Canadian antidumping laws, strongly favoured the retention of zeroing. However, the U.S. Department of Commerce used zeroing against Canadian softwood lumber to achieve substantially higher dumping margins than otherwise would have been attainable. The Canadian softwood producers urged the Canadian Government to challenge the U.S. practice of zeroing before the WTO. The Canadian Government acceded to the wishes of the softwood producers and launched a successful challenge against the United States. Canada could not creditably condemn the U.S. practice of zeroing while the CBSA continued to zero. The CBSA has now formally reversed its former policy and has announced that its current policy is to subtract the total export price from the total normal value of all goods shipped to Canada during the period of investigation, including individual sales made at undumped prices.

Policy and Practice Implications

There is no doubt that the CBSA's decision is correct, both as a matter of domestic law and under Canada's international obligations. The decision will result in a fairer application of Canada's antidumping laws than in the past but will make it more difficult for domestic producers to achieve effective protection against import competition through the imposition of antidumping duties.

[2] *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India*, Panel Report WT/DS141/R 30 October 2000, Appellate Body Report, WT/DS141/AB/R 1 March 2001.

Participation In The Investigation

The CBSA allowed interested parties to participate much more extensively in the investigation process than has been the case under past practice. Previously, once the CCRA or the Deputy Minister commenced a dumping or subsidy investigation, exporters completed questionnaires and the CCRA or the Deputy Minister conducted verifications and completed dumping or subsidy calculations with virtually no input from other interested parties such as the complainant and other domestic producers, as well as importers. This practice changed following the decision in 2004 of the Federal Court in *Canadian Steel Producers Assn. v. Canada*[3]. The CBSA now posts a list of all exhibits submitted during the course of its investigation on its website and counsel who have filed confidentiality undertakings have access to any exhibit posted on the website. Exhibits include protected copies of exporters' questionnaire responses. In the *Laminate Flooring* case, the CBSA also circulated copies of its final dumping and subsidy calculations to all counsel who had filed confidentiality undertakings before they were released and invited comments.[4]

Policy and Practice Implications

The CBSA's current policy is much more transparent and, within the confines of the very tight statutory time limits under which the CBSA must make its dumping and subsidy determinations, provides an opportunity for the domestic industry and importers to influence the outcome of these determinations that previously did not exist. However, this raises some practice issues. Fee competition in antidumping and countervailing duty cases is intense. Practitioners who act for domestic producers or importers now have to factor in time for participation in the CBSA investigation process. Counsel must consider the chances that actively participating will have a material effect on the ultimate outcome of the dumping or subsidy determination and advise the client accordingly. Full participation, which would entail reviewing exporter questionnaire responses, could be immensely time-consuming. Partial participation would entail filing submissions and comments when invited by the CBSA to do so, without reviewing every exporter questionnaire response. Clients must be advised that these opportunities to participate exist but must be cautioned that meaningful participation could substantially increase the fees that they would have to pay.

Chinese Subsidy Programs

Since the *Automotive Laminated Windshields* case in 2002[5], the CBSA has treated China as a market economy unless there was evidence that prices and costs of the particular industry under consideration were shown to be under state control.

Previously China was treated as a non-market economy in which prices and costs are determined by the state rather than by market forces. The CBSA follows the practice common to antidumping agencies in other

[3] [2004] 2. F.C.R. 642. This case decided that the complainant in a dumping investigation and its supporters were interested parties whose counsel were entitled to access to confidential information filed by exporters. This case did not deal with the rights of counsel for importers to such information, but the same logic applies, given that importers receive and complete Requests for Information from the CBSA and are directly affected by the outcome if dumping is found.

[4] Despite the substantial access granted by the CBSA, the complainant was not satisfied and has applied to the Federal Court of Appeal for judicial review, claiming that the CBSA failed to observe principles of natural justice and procedural fairness. See Court File No: A-285-05.

[5] The Statement of Reasons concerning the final determination of dumping in this case were released on July 31, 2002.

countries in dumping investigations involving imports of non-market economies of choosing a surrogate country at a similar stage of development to the state controlled country but with a market economy. Normal values are based on selling prices or costs in the surrogate country. The predecessors to the CBSA did not conduct subsidy investigations respecting imports from non-market economies because the enterprises producing the imported goods are themselves owned or controlled by the state.

The CBSA's Subsidy Investigation

With imported Chinese goods now being produced by privately owned firms charging prices and being subject to cost structures determined by market forces, domestic complainants in Canada began alleging that private firms in China were being subsidized by the Chinese Government in a variety of ways. The CBSA's first subsidy investigation was in the *Barbeques* case in 2004. The investigation disclosed a rate of subsidy below the *de minimis* two percent rate threshold that applies to developing countries such as China and the investigation was terminated. The second subsidy investigation occurred in the *Fasteners* case. The CBSA considered that the information that it received from the Government of China was not complete and determined a subsidy rate of 31.53% of the export price in accordance with a ministerial specification.[6] The CBSA's most recent subsidy investigation occurred in *Laminate Flooring* in which the CBSA received complete information from the Government of China.

The CBSA's Statement of Reasons in *Laminate Flooring* provide a number of insights into both the subsidy programs that exist in China that are potentially vulnerable to countervailing duties and the expansive view of specificity that has been adopted by the CBSA in considering whether these programs can be countervailed. A Summary of Actionable Subsidy Programs is set out in Appendix 3 of the CBSA's Statement of Reasons. Despite the fact that the list of actionable subsidy programs is quite lengthy, the overall rate of subsidy found for laminate flooring imported from China was only 3% of the export price.

Over the protestations of the complainant, the CBSA refused to consider China's fixed exchange rate system as a subsidy. This refusal was entirely correct. Exchange rate controls do not fit within any of the categories of "financial contributions" listed in the WTO Subsidies and Countervailing Measures Agreement that can form the basis for an actionable subsidy.

Preferential Tax Programs

Most of the subsidies found by the CBSA to be actionable were preferential tax programs of various sorts involving both income taxes and value-added taxes (VAT). Tax relief in any form can form the basis for an actionable subsidy if the tax relief benefits "certain industries" or "certain enterprises" and is, therefore, "specific".

1. FIEs and DIEs

Under Chinese law, an FIE is a foreign invested enterprise and a DIE is a domestic invested enterprise. An FIE can be wholly foreign owned or be a joint venture with at least 25% foreign ownership. Many Chinese tax programs provide more favourable treatment to FIEs than to DIEs. For example, FIEs engaged in certain "productive enterprises" receive tax relief for up to ten years. FIEs receive tax relief for operating in industries and sectors where foreign investment is encouraged by the state. FIEs receive refunds of income tax on

[6] Section 30.4(2) of the Special Import Measures Act confers broad discretion to determine the amount of subsidy when the CBSA has received insufficient information. The amount of subsidy is to be determined "in such manner as the Minister [of National Revenue] may specify", and hence the expression "ministerial specification".

reinvested profit, as well as exemption on tariffs and VAT on imported equipment. These tax programs are either not available to DIEs or the availability is restricted.

While some of these programs relate to specific industries, others can apply to any industry. Nonetheless the CBSA considered that these preferential tax programs were specific because FIEs could be considered to be a "group of enterprises", even though they did not produce the same products. In making this decision, the CBSA rejected counsel's submission that the CBSA's position was inconsistent with Canada's position before a WTO panel in *United States – Final Countervailing Duty Determination With Respect to Certain Softwood Lumber from Canada* by pointing out that the WTO panel in that case had rejected Canada's position. The CBSA also stated that it did not regard program eligibility based on the nature of a firm's ownership as representing an objective criteria or condition.

While not indefensible, the CBSA decision interprets the concept of specificity very broadly. Interestingly, Canadian income tax law also provides preferential treatment based on nationality, except that it is domestically controlled enterprises that receive the preference. Based on the CBSA's logic, the small business deduction, which can only be utilized by Canadian controlled private corporations, would be an actionable subsidy that could be countervailed.

2. Special Economic Zones

China makes use of special economic zones, within which enterprises, whether FIEs or DIEs, pay income taxes at lower rates than those that apply generally. Counsel argued that if all enterprises within a specific geographic area were subject to the same rate of tax, the preferential treatment should not be considered as specific. The CBSA decided that preferential tax treatment provided in the special economic zones constituted specific subsidies because the granting authority, being the central government, was providing tax rates in the special economic zones lower than the tax rates that it provided generally. If the geographic area comprising the special economic zone had its own granting authority (such as the government of a Canadian province in respect of that province) that applied the same tax rate throughout the area, the CBSA would not have considered the tax treatment as specific, even though it was more favourable than in other parts of the country.

Policy and Practice Implications

The *Fasteners* and *Laminate Flooring* cases have demonstrated that it is possible to secure countervailing duties against Chinese imports. However, the significant difference between the two cases is that in *Laminate Flooring*, the Chinese Government provided complete information while in *Fasteners*, the Chinese Government did not provide information to the extent that the CBSA considered necessary. In *Fasteners* the overall subsidy rate of 31.53% is high, while the overall subsidy rate of 3% in *Laminate Flooring* is low. Both exporters and importers should take note that the results are vastly more favourable when exporters and the Chinese Government provide complete information, as occurred in *Laminate Flooring*. Domestic producers should take note that despite the long list of subsidies considered actionable, a countervailing duty based on subsidy rate of only 3% will provide minimal protection against imports from a country with many real cost advantages, like cheap labour.

Importers should be mindful that producers and exporters in China who are DIEs fared better than producers and exporters who are FIEs because of the preferential tax treatment that FIEs receive. However, the overall low rate of subsidy in *Laminate Flooring* does not suggest that the risk of countervail when importing from an FIE as opposed to a DIE is very great.

The CBSA was not swayed by counsel's arguments based on Canadian practice or Canadian positions taken in past WTO cases. In my view, from a policy perspective the CBSA should have paid more attention to those

factors given that Canadian domestic policy encompasses both regional development programs (which have some similarity to special economic zones) and preferential tax treatment based on nationality. The U.S. Department of Commerce would have no hesitation in using CBSA decisions applying a broad interpretation of specificity requirements in U.S. subsidy investigations against imports from Canada.

The Chinese Government should be generally satisfied with the result, given the overall low rate of subsidy. The Government is currently considering a tax reform proposal that will apply the same income tax rates to DIEs and FIEs. If this reform goes into effect, there will no longer be a basis for countervailing duties based on preferential tax treatment of FIEs.