PUBLIC
109 FILE

John O'Connor and Associates Pty Ltd

(ABN 39098650241)

PO Box 329
Coorparoo QLD 4151
Telephone: 07 33421921
Facsimile: 07 33421931
Mobile: 0411252451
Email: jmoconnor@optusnet.com.au

2 April 2012

Mr Michael Kenna
Case Manager, Operations 3
International Trade Remedies Branch
Australian Customs and Border Protection Service
Customs House
5 Constitution Avenue
CANBERRA ACT 2601

For Public File

Dear Mr Kenna

Structural Timber exported from Austria, Canada, Czech Republic, Estonia, Germany, Lithuania, Sweden and the USA – Applicants' Response to Statement of Essential Facts No. 176

Please find attached on behalf of the Applicant companies a Public File version response to Statement of Essential Facts ("SEF") No. 176 on structural timber exported from Austria, Canada, Czech Republic, Estonia, Germany, Lithuania, Sweden and the USA.

If you have any questions concerning the attached submission, please do not hesitate to contact me on (07) 3342 1921.

Yours sincerely

John O'Connor

John O'Connor
Director

Cc Mr Tim Sherry, CHH Woodproducts Australia
Ms Christine Briggs, Gunns Timber Products
Mr Chris Robertson, Hyne and Sons

Executive Summary

In this submission in response to SEF No. 176, the Applicant companies[1] reject the Australian Customs and Border Protection Service ("Customs and Border Protection") assessment of dumping margins determined for all exporters of the goods under consideration ("GUC") from the nominated countries (with the exception of margins determined for Ilim) as the basis for determining normal values (whether on basis of s.269TAC (1) or s.269TAC (2)(c) as appropriate). The SEF fails to accurately reflect the domestic selling price and/or cost to make and sell the GUC exported to Australia.

The incorrect identification of the relevant and appropriate costs to make and sell the GUC materially understates the preliminary dumping margins determined. It is the Applicants' position that had the correct and relevant costs been identified, positive dumping margins above negligible levels for exports of the GUC from the nominated countries would have been determined.

Further, the Applicants do not concur with Customs and Border Protection's assessment that sales by Stora Enso associated companies in the relevant exporting country (i.e. Austria, Czech Republic, Estonia, Lithuania and Sweden) to the Australian importer, Stora Enso Timber Australia Pty Ltd ("SETA") are arms length sales, as it is considered certain corporate and selling expenses that are outside the legal entities investigated are not fully reflected in the export price determined.

Once full account of the relevant costs of production and the appropriate methodologies are applied to the GUC have been identified for all exporters, and the arms length nature of certain export sales to Australia (by Stora Enso associated companies) have been re-evaluated, positive dumping margins above negligible levels for the GUC will be evident.

Introduction

On 13 March 2012, Customs and Border Protection released Statement of Essential Facts ("SEF") No. 176 in respect of investigations into the alleged dumping of certain structural timber exported from Austria, Canada, the Czech Republic, Estonia, Germany, Lithuania, Sweden and the USA.

Customs and Border Protection's investigations with co-operative exporters determined that exports of the ("GUC") from Austria, Canada, the Czech Republic, Estonia, Lithuania, Sweden, the USA, and by Egger Sagewerk Brilon GmbH ("Egger") were at non-dumped prices. Exports of the GUC by Ilim Timber HWN Holz Werke Nord GmbH ("Ilim") of Germany were at dumped margins of 15.7 per cent.

SEF No. 176 states that the dumped imports by Ilim accounted for sales in Australia of less than 2 per cent of the total Australian market for the GUC over the investigation period[2]. Customs and Border Protection commented that Ilim's exports "*have not been increasing in volume, are largely directed at niche markets within Australia and have not shown a pattern of undercutting undumped imports in the Australian market.*[3]"

Customs and Border Protection has therefore preliminarily concluded that "*there has been dumping of some or all of the structural timber exported from Germany but that the injury, if any, to the Australian industry that has been or may be caused by that dumping is negligible*"[4].

SEF No. 176 includes a proposal to terminate the investigation for all exporters of the GUC from the nominated countries.

[1] Building Supplies Group Holdings Pty Ltd (BSG), Hyne and Sons Pty Ltd, and Gunns Limited.
[2] Investigation period is 1 July 2010 to 30 June 2011.
[3] Statement of Essential Facts No. 176, P.7.
[4] SEF No. 176, P.41.

PUBLIC
107 FILE

Dumping Investigation

(i) Exporter Visit Reports

The Applicants have provided submissions in response to each of the Exporter Visit reports for all cooperative exporters that have been placed on the electronic public file. The Applicants do not retreat from the comments as detailed in response to each exporter visit report and maintains the validity of the comments (although the comments have not been reflected in SEF No.176). These comments are specific and relate particularly to the circumstances of each exporter.

(ii) Review by cost accounting experts

At Section 6.5 of SEF No. 176 Customs and Border Protection outlines the basis of the appointment of the KPMG "*to undertake an independent review of the procedures followed and evidence reviewed during visits to three exporters to Australia, Stora Enso Eesti AS of Estonia and the two Stora Enso entities in the Czech Republic*". The purpose of the review was "*to consider whether the verification undertaken by Customs and Border Protection was adequate, and whether the cost data verified were reasonable and reliable for the purposes of determining normal values.*"

The Applicants are not seeking to contest whether the information reviewed by KPMG was "reasonable and reliable". What is contested, however, is an absence of knowledge of the appropriate treatment of costs for the GUC <u>at the time of the conduct of the exporter verification process</u>, not whether the cost data verified post the verification was reasonable and reliable.

The Applicants understand that the KPMG review did not involve an "independent expert" with relevant industry knowledge concerning the identification of costs and treatment of credits for determining the cost-to-make-and-sell the GUC.

(iii) Review by timber industry experts

Customs and Border Protection references the engagement of "*industry experts who together have extensive experience in timber industry accounting practices and sawmill operations*" to review the exporter visit reports and one submission by the Applicants in response to Stora Enso Lithuania's public file Exporter Visit report.

The Applicants' have reviewed the independent experts report placed on the public file dated 10 February 2012. The document confirms the objective of engagement of the independent experts and the scope of the analysis. The scope limitations indicate that the independent consultants did not examine areas covered by the KPMG Report or the "*procedures covered by C&BP during exporter visits*".

The approach followed by the independent experts is also detailed in the Report, including:

- Reviewing the exporter visit reports for all identified exporters;
- Reviewing in detail documents, operational data and cost data provided by C&BP for four exporter operations;
- Reviewing C&BP's 'like goods' assessments and findings for all identified exporters;
- Testing of selected data, calculations and models prepared by exporters and C&BP, including cost allocations and arm's length transactions;
- Interviewing C&BP staff who conducted exporter visits and who prepared the exporter visit reports;
- Comparing selected areas of sawmill operations and cost accumulation to industry benchmarks and industry practices.

The review conducted by the industry experts was limited by the information <u>sourced</u> by Customs and Border Protection obtained from each of the cooperative exporters and adequate time. The independent experts would not able to advise Customs and Border Protection as to the relevant information to be sourced from the exporters prior to the visits.

It is anticipated that Customs and Border Protection would have notified the industry experts that the information obtained was in accordance with the generally accepted accounting principles ("GAAP") in the country of export. The Applicants do not contest this issue. However, the allocation of costs in respect of the GUC as addressed by the Applicants in response to each of the exporter visit reports is also in accordance with GAAP. The independent experts were provided with limited time to review the information following the completion of the verification visits; they were not provided with the opportunity to advise on the appropriate and relevant costs to be adequately satisfied as to the specific costs for the GUC; nor conduct a considered review of the Applicant's responses to the Exporter visit reports.

The industry experts noted a number of items following their five-day review. The comments are included at Section 2 of the Report. The Applicants observe that the industry experts alerted Customs and Border Protection to the treatment of residue credits by Stora Enso in the Czech Republic. The residue credits were not offset against log costs, as was the practice in other countries. The industry expert report indicates that the treatment by Stora Enso was "*in line with Czech accounting standards*".

On 17 February 2012, Customs and Border Protection issued an addendum to the Stora Enso Wood Products Plana S.R.O and Stora Enso Wood Products Zdirec S.R.O Czech republic Exporter Visit Report. The addendum reversed Stora Enso's treatment of the residue credits and included these against production costs. The reasoning for doing this, as asserted by Customs and Border Protection, was to bring the treatment for Stora Enso Czech Republic in alignment with the practice of all other exporters under investigation. By doing so, the costs for the GUC as exported by Stora Enso from the Czech Republic are not in accordance with GAAP in the Czech Republic (as required by Regulation 180 (2)(b)(i)).

The Applicants highlight that Customs and Border Protection had previously reported the applicable dumping margin for Stora Enso Czech Republic based on GAAP in that country, and now the revised dumping margin does not reflect GAAP in the Czech Republic. Determined dumping margins for Stora Enso Czech Republic are at odds with the required practice of accepting costs that are in accordance with GAAP in the country of export.

The Applicants also note that the industry experts identified additional areas that were brought to the attention of Customs and Border Protection, including:

- Related party sales of woodchip by the Stora Enso Napi mill in Estonia were at higher prices than sales to unrelated parties – no apparent action was taken as the industry experts were told by Customs and Border Protection that the difference was "not material"
    - Additional concerns were also raised in respect of sales of woodchip by the Stora Enso Brand mill in Austria that represented a high proportion of revenue;
- Comment by Stora Enso Lietuva Lithuania in relation to the value of small logs that was "counter to industry experience"; and
- Packaging costs for the Stora Enso Czech mills does not separately record domestic and export costs.

Customs and Border Protection moved swiftly to adjust the Stora Enso Czech Republic treatment of residue credits and amend dumping margins (favourable to exporter). This change to the treatment of residue revenues, however, is inconsistent with the GAAP in the Czech Republic.

The Applicants' are unclear as to whether the comments of the industry experts have been addressed by Customs and Border Protection and the subsequent impact on the preliminary dumping margins determined.

The review of the information obtained by Customs and Border Protection and provided by the relevant cooperative exporters does not allay the Applicants' concern that the verified CTM&S for the GUC is inaccurate. As will be discussed below, the verified information is unspecific concerning the exported GUC.

(iv) Benchmarking of costs

SEF No. 176 refers to the report titled Global Timber/Sawmill/Lumber Cost Benchmarking Report – 2010 Annual Basis and Q1/2011 (i.e. "Benchmarking Report"). The Applicants referred to the Benchmarking Report in its application and in exporter briefing documents provided to Customs and Border Protection prior to verification visits with cooperative exporters.

The Benchmarking Report details by country certain costs including log, sawmill, overheads and revenues including woodchip, to provide details of margins for participating countries.

Whilst the Benchmarking Report provides guidance on average sawmilling costs, including a breakdown of costs through some production phases, it does not provide production costs for MGP grade structural timber (i.e. the GUC).

(v) Submissions by Applicants

As indicated, the Applicants provided submissions in response to each Exporter Visit Report placed on the public file. The submissions address the costs (and revenues) associated with the cost-to-make-and-sell ("CTM&S") MGP grade structural timber (i.e. the goods exported to Australia).

The submissions raise concerns about the treatment of certain costs and whether sufficient inquiries were made of exporters by Customs and Border Protection as to how the verified costs were determined[5].

SEF No.176 is silent on the range of issues raised by the Applicants in each submission other than to state that in relation to the verified costs "*there were no grounds upon which to require exporters to calculate the product cost to a level of detail not supported by their accounting or management records or industry accounting practices, both in Australia and overseas*"[6].

The comments referred to by Customs and Border Protection that there were no basis to require the exporters to provide costs for the GUC to a level of detail not supported by their accounting or management records are concepts central to the concerns of the Applicants. Similarly, the assertion that the Australian industry does not provide this level of detail for costs is not an accurate reflection of the reporting standard of the industry. These matters are addressed below.

Costing methodologies

The Applicants have submitted that the exporters have not provided CTM&S data for the goods exported to Australia (i.e. for MGP grade structural timber). Rather, the costs verified by Customs and Border Protection during verification visits conducted at the exporters' premises represent average costs of processing timber through the sawmilling, drying and planing processes.

It is further suggested by Customs and Border protection that it is unreasonable for the exporters to provide costs beyond what is required or contained in the general accounting or management records of the entity the subject of the verification visit.

[5] Refer separate Applicant responses to Exporter Visit reports.
[6] SEF No. 176, P.22.

SAP ERP

It is noted that Stora Enso is a progressive global paper and timber manufacturing company. The company uses SAP enterprise resource planning ("ERP") as its accounting information system[7] and are not alone in their use of SAP or like system by the Exporters. Company reporting is via Hyperion Financial Management. The SAP Accounting System used by the Stora Enso entities is able to produce standard cost reports[8] for timber products manufactured at each of the manufacturing sites that export the GUC to Australia. Specifically, Stora Enso would utilise the SAP capability to prepare standard cost reports for MGP grade structural timber, along with other specific timber products manufactured on site (including structural timber produced to European Structural Standards).

The Australian Applicant companies – unlike the Stora Enso companies in the nominated exporting countries – are dedicated to the production of structural timber. The Applicant companies, therefore, seek to produce high-grade structural timber to MGP specification at <u>all</u> times. At the [*company*] industry verification visit, Customs and Border Protection was provided access to all standard cost reports to produce MGP grade structural timber [*site*]. Customs and Border Protection selected the standard cost for MGP [*xx*] grade structural timber[9] for the September 2010 quarter for verification.

The Applicants therefore reject Customs and Border Protection's statements in SEF No. 176 that the Australian industry does not prepare accounting or management records for the GUC (i.e. MGP grades of structural timber). Further, the Applicants' actual financial data reflects an objective to produce 100 per cent structural timber output contest that all structural timber manufacturers in Australia prepare standard costs for MGP structural timber.

The Applicants highlight with Customs and Border Protection that cooperative Stora Enso manufacturing exporters utilise the SAP ERP System and this system is used for preparing standard cost reports for processed timber (including MGP grade structural timber). It is unclear from the Stora Enso Exporter Visit Reports why the exporters did not provide Customs and Border Protection with applicable standard cost and work order variance reports for MGP grade timber for the investigation period given that this information would be readily available from their SAP ERP system to assist in the verification of the CTM&S the MGP grade structural timber exported to Australia.

Downgrade Loss (including residues)

The Applicants have detailed in submissions to Customs and Border Protection that the production costs for MGP timber are higher than other commonly manufactured timber products. The dumping margins determined for the cooperative exporters do not reflect higher unit costs for MGP production exported to Australia (with the possible exception of Eggers and Vaagen). The higher MGP costs are driven by such factors as drying and planing, as well as taking full account of downgrade losses (i.e. product that is rejected following the MGP production phase and does not meet MGP standard and is often termed "B Grade" product).

Customs and Border Protection has stated in SEF 176 that it has accepted the exporters' treatment of B Grade product as a "joint product" and not a "co-product". This approach has ramifications for the cost of production for MGP grade timber. If treated as a joint product, the losses on downgrade product are not taken into account in producing MGP grade timber. Customs and Border Protection has further stated that that it "*does not see any grounds to compel the overseas exporters to apply losses on B grade timber to the goods under consideration*"[10].

[7] Refer Stora Enso Wood Products Czech Republic Exporter Visit Report, P.11; Stora Enso Austria and Sweden Exporter Visit Report, P. 11 & 12; Stora Enso Lietuva UAB Alytus Sawmill, Lithuania Exporter Visit Report, p.9; Stora Enso EESTI AS (NAPI) Estonia, Exporter Visit Report.
[8] Refer www.sapebooks/info/controlling/moving-average-price-vs-standard-price/
[9] Refer
[10] SEF No. 176, P.22.

The treatment of the losses on downgrade product by referring to B Grade structural timber as a "joint product" is inconsistent with the manufacturing process and treatment of residue credits by the exporters (and accepted by Customs and Border Protection). It is common practice in the industry to include downgrade losses (including residue credits) on a return to log basis when costing the target products (e.g. the GUC). The alternative is to exclude all residues and downgrade product to cost all target output. It is therefore inappropriate to apply a mixture of these two methodologies – as has been applied to the cooperative exporters.

The acceptance by Customs and Border Protection of the exclusion of downgrade losses on B Grade timber arising from the manufacture of the GUC is out of step with the inclusion of residue credits offset against the cost of log. By disregarding the downgrade losses, a consistent application of the appropriate methodology in this instance would also involve excluding the residue credits.

Conversion costs

The specific losses through the drying and planing mill should also be included in the cost of MGP. It is the Applicants' understanding that the average sawmill recovery is approximately xx per cent for timber, however, in MGP production the recovery is approximately xx per cent – there is a xx per cent differential between the average mill cost and the average MGP cost. These losses are also attributed to the production cost of MGP exported to Australia. It is not clear whether Customs and Border Protection has adequately considered actual drying and planing mill losses for the GUC across all exporters.

The Applicants strongly contest that SEF No. 176 is incorrect with respect to costing methodologies:

- in asserting that it is unreasonable for exporters to provide specific product costings for MGP grade product exported to Australia when Stora Enso plants operate SAP ERP systems that produce standard cost reports;
- as [*company*] provided Customs and Border Protection with standard cost reports for MGP grade timber at verification visit;
- with the inconsistent approach on the acceptance of the exporters' practice of treating downgrade MGP as a joint product, but also allowing for the inclusion of residue credits as an offset against input log cost.

Representative log basket

In response to certain exporter visit reports (including Vaagen, Teal Jones, Western Forest Products, S E Lithuania) the Applicants identified that Customs and Border Protection appeared to have undertaken a partial evaluation of fibre used in the manufacture of the GUC. These comments were made to ensure the cost to make the GUC was not constructed on a price of a non-representative lower cost log, size or quality.

It was noted by the Applicants that there existed an absence of discussion on actual log quality and diameter class used for the GUC and how this compared with the site average and the GUC CTM&S.

The Applicants view the inclusion of non-representative log as a contributing factor to the dumping margins determined (particularly in Canada, the USA, Lithuania) where it is evident that lower CTM&S for the GUC has been verified and accepted by Customs and Border Protection.

Smaller diameter log

The Applicants' highlighted with Customs and Border Protection that small log recovery gain is counter to international mill experience, including that of the Australian industry. The Applicants submitted that using small logs for the GUC was unlikely to achieve the Global Timber/Sawmilling Benchmark Report yield rate of xxxx%, whilst incurring additional processing cost above site averages, particularly when producing MGP structural planed timber with tighter specification. It was stated that the reduced yield has a significant impact on CTMS for GUC, with higher losses apparent.

The Applicants provided Modelling that supports this position and critically highlights the need to examine both end to end cost by product as opposed to averages (See Confidential Attachment 1).

Ultimately it is industry experience that the processing costs for a smaller diameter log are higher than for a large diameter log based on lower yield from log.

Arms length purchases and sales

In its response to the Stora Enso Lithuania Exporter Visit Report the Applicants highlighted a range of concerns that must be considered in assessing whether the export prices to Australia for the GUC may be considered arms' length transactions.

The industry experts commented on the information obtained by Customs and Border Protection in the exporter visit reports.

The applicants, however, are concerned that not all costs incurred by Stora Enso Oyj Finland and its affiliated companies are reflected in the Group's activities associated with the sale of the GUC exported to Australia. The Attached Stora Enso Organisation Chart (Non-Confidential Attachment 2) highlights a range of corporate support functions that apply across the Stora Enso Group of companies. The exporter visit reports for each of the Stora Enso entities exporting from the nominated European countries do not (publicly) disclose whether the costs associated with the corporate functions have been allocated to the GUC.

Further, it is noted in certain reports that Stora Enso affiliates provided raw materials and distribution services to some exporting mills. The reports are silent as to the level of trading support provided by the Stora Enso parent and its affiliated companies to exporters of the GUC (and to the affiliated Australian importer).

Material injury and causal link

SEF No. 176 confirms that the Australian industry has suffered material injury during the investigation period in the form of:

- reduced sales volumes;
- reduced market share;
- price depression;
- price suppression;
- reduced profits;
- reduced profitability;
- reduced production volume;
- reduced revenue;
- reduced employment;
- underutilised production capacity;
- deteriorating returns on investment; and
- reduced ability to attract investment.

Customs and Border Protection has preliminarily concluded that the non-dumped imports were the cause of injury to the Australian industry as the market share increased from 14 to 23 per cent between 2007/08 and 2010/11.

The dumped imports from Germany also account for between 1 and 2 per cent of the Australian market.

Conclusions

This submission addresses certain shortcomings with Customs and Border Protection's verification of exporters' costs of the GUC during the investigation period. The identified concerns materially impact the dumping margins determined for each cooperative exporter. The acceptance of average sawmill costs for MGP exported to Australia that do not reflect the higher MGP cost of production, understates the CTM&S the GUC. Further, the inconsistent approach followed to exclude downgrade losses from MGP production costs whilst allowing residue credits to be offset against log costs, does not enable a true cost of MGP grade structural timber to be established for each exporter. Similarly, it is unclear whether drying and planing losses have been correctly accounted for.

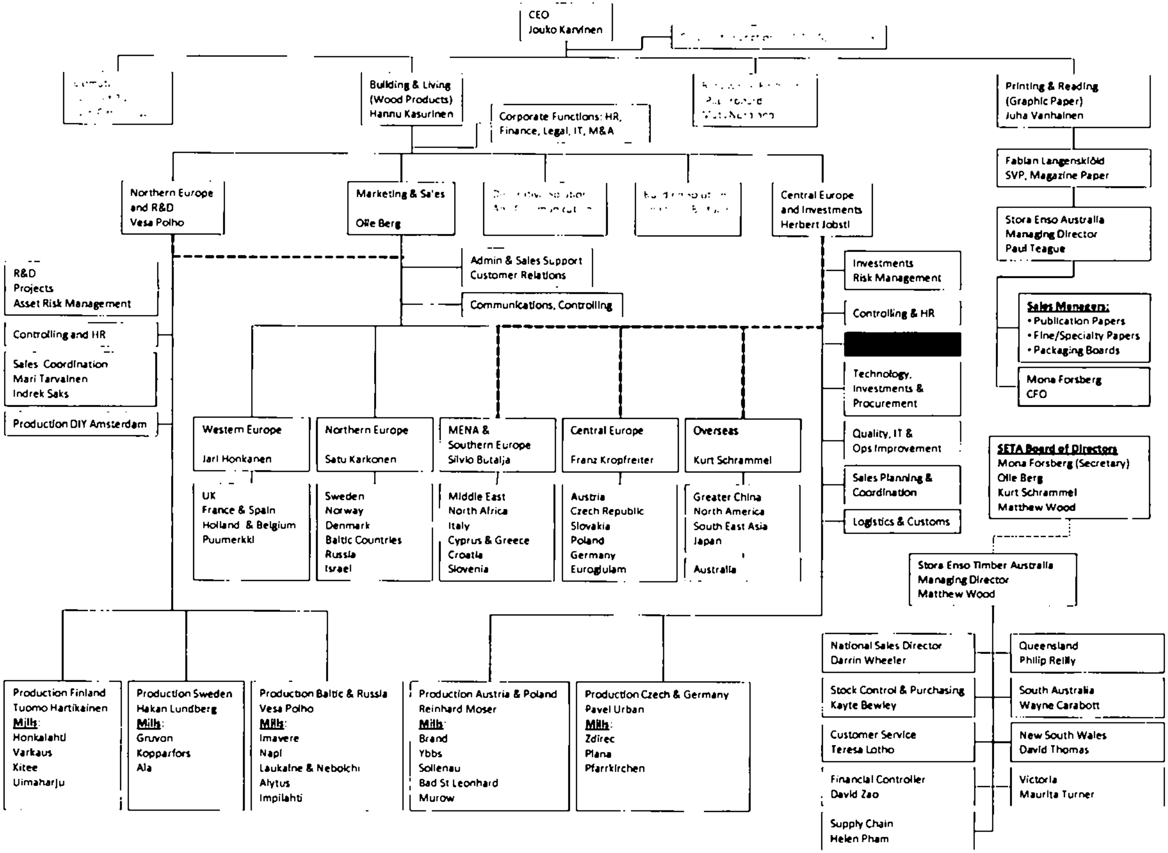
Had Customs and Border Protection has been provided with access to SAP ERP generated standard cost reports and work order variance reports for MGP produced by each exporter, it would have been better positioned to verify the costs associated with MGP structural timber exported to Australia.

The Applicants request Customs and Border Protection to:

- request and review standard costs for MGP manufactured by each of the cooperative exporters and associated work variation reports;
- address the inconsistent approach of categorising downgrade product as a joint product to MGP (thereby excluding the downgrade losses from MGP production costs) and the inclusion of residue credits as offsets to log costs;
- address the matters raised by the industry expert's including the return on small diameter logs used in MGP production, and packaging costs for Stora Enso Czech Republic;
- ensure that the CTM&S the GUC exported by Stora Enso in the Czech Republic reflect costs maintained in accordance with the accounting standards in the country of export; and
- review whether sales between the Stora Enso export entities and the related Stora Enso Timber Australia are arm's length transactions and whether the Stora Enso Group of affiliated companies provides any financial support to the companies exporting the GUC or to the Australian importer.

A comprehensive re-examination of the above matters will impact the dumping margins determined for all cooperative exporters. The revised dumping margins will further influence Customs and Border Protection's preliminary view that dumping has not caused material injury to the Australian industry producing MGP structural timber.

An increase in the volume of structural timber imports from the nominated countries at dumped prices following a re-examination of the issues identified in this submission will result in dumped and injurious imports at above negligible levels.



PUBLIC
100 FILE