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PUBLIC FILE VERSION

7 February 2012

Mr Justin Wickes
National Manager
International Trade Remedies Branch
Australian Customs & Border Protection Service
Customs House
5 Constitution Ave
CANBERRA ACT 2601

Dear Mr Wickes

Re: Trade Measures Enquiry No 176 – Structural Timber Exported from Austria, Canada, the Czech Republic, Estonia, Germany, Lithuania, Sweden and the USA

We act for Ilim Timber HWN Holz Werke Nord GmbH ('Ilim Timber') being an exporter of structural timber from Germany to Australia.

Ilim Timber has cooperated fully with the Australian Customs and Border Protection Service ('Customs') in relation to this investigation. Customs visited our client in late November and early December 2011 and have prepared an Exporter Visit Report. We note that our client has been provided with a draft of the Exporter Visit Report ('Visit Report') and has provided feedback to Customs on the matters contained in the Visit Report.

Despite this, there are several issues that our client has raised with Customs that have not been taken into account in the Visit Report. This is important because the issues raised by our client are likely to have an impact on the calculation of any dumping margin, which at present is found by Customs to be 15.7 percent.

It is important to note that Ilim Timber's exports to Australia in the investigation period were

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[CONFIDENTIAL TEXT DELETED - VOLUME DETAILS] (see Visit Report Section 6.2) out of total Australia sales of construction timber of approximately 1.8million cubic metres. This represents approximately [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent of the total market for the GUC. Ilim Timber's exports to Australia in the investigation period comprise about [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent of total imports to Australia.

Our client wishes to draw to the attention of Customs the following matters:

1. The use of an excessive profit margin in calculating domestic sales profit

Customs has determined that there are no comparable sales of like goods in our client's case because structural timber sold by Ilim Timber in Germany is predominantly spruce, whereas exports to Australia are pine.

Customs have therefore moved to a constructed normal value for domestic sales pursuant to s269TAC(2) of the Customs Act.

In paragraph 11.2 of the Visit Report, Customs has determined a profit margin on domestic sales of [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent.

However, Customs has erroneously based this profit calculation on a premium spruce construction timber sold in Germany that is very different from the pine structural timber exported to Australia. These premium spruce products are listed in Appendix 2 of the Visit Report, 'ordinary course of trade and profit calculations' under the tab 'SAPBW - Download'. The product examined by Customs is known as 'F1HW2 KD 15' and it is a thick timber, often used for house beams. This product is generically referred to as 'KVH'. Ilim Timber's average sale price of this product is approximately [CONFIDENTIAL TEXT DELETED - PRICE FIGURE] Euros per cubic metre.

It is not possible to establish a profit margin based on like goods under Customs Regulation 181A(2) because there are no like goods. The product sold to Australia is a pine product sold in much smaller sizes and it is much less expensive than the spruce premium product. It is extremely inconsistent for Customs to state that there are no like goods for the purposes of using actual domestic sales to establish normal values, but Customs has seen fit to say that the spruce construction timber is a like good for establishing a constructed normal value profit margin.

To elaborate further, there are many reasons why it is inappropriate to compare German spruce construction timber with Australian exports to determine a constructed normal value. Factors include:

- Spruce is a more expensive product;

- German construction timber is of larger dimensions and requires a bigger diameter and higher quality log for sourcing;
- Spruce is more visually attractive (e.g. fewer knots and bends) and does not discolour;
- It is used for big beams which are critical for construction and for which purchasers are prepared to pay a large premium;
- Spruce logs generate both higher value and lower value (i.e. packaging) timbers which are sold on the domestic market, whereas pine logs sourced for Tilling are all converted to the various grades exported to Australia.

None of the above factors apply to the pine products exported to Australia.

The essential point is that the profitability of this premium spruce construction timber is much higher than if Ilim Timber was selling pine construction timber within Germany. To illustrate this point, we note that whilst the average price of the premium product is [CONFIDENTIAL TEXT DELETED – PRICE FIGURE] Euros per cubic metre, the average price per cubic metre for all domestic sales is [CONFIDENTIAL TEXT DELETED – PRICE FIGURE] Euros, and the price per cubic metre of domestic products that are of similar sizes to that sold to Australia is [CONFIDENTIAL TEXT DELETED – PRICE FIGURE] Euros. As the cost to make and sell is [CONFIDENTIAL TEXT DELETED – RELATIONSHIP OF PRICES], it is clear that Customs have selected [CONFIDENTIAL TEXT DELETED – LEVEL OF PROFITABILITY] product Ilim Timber sells and has applied this margin to determine a potential profit for establishing normal value. We are instructed that European timber producers would be enjoying relatively spectacular profitability if this was a representative profit across their businesses. This is not the case as shown by the [CONFIDENTIAL TEXT DELETED – LEVEL OF PROFITABILITY] margins Ilim Timber achieves for domestic sales.

The average prices for domestic sales are set out in **Confidential Attachment 1 – ‘German Volumes per company DE 08 2010-06 2011 (V2)’** which is attached to this submission.

It is therefore more appropriate to apply a profit margin that applies to domestic sales generally in the investigation period rather than one non-like premium product. Ilim Timber did provide Customs with sales information concerning German construction timbers that were of similar sizes and that were planned, but the sample was too small for Customs to accept this information.

Customs is aware, based on Ilim Timber’s audit reports provided to it, Ernst Young’s confirmation that the economic environment for the entire saw mill industry is difficult. Our client did not record a profit in its accounts for the period from 1 July to 31 October 2010.

It is our client’s position that no profit margin should be applied in calculating a normal value. This can be approximately demonstrated by comparing the average prices of Ilim Timber’s domestic sales with the CTMS established by Customs. The average CTMS for unplanned spruce timber across Q1 – Q4 is [CONFIDENTIAL TEXT DELETED – PRICE FIGURE] Euros,

whereas the average price of unplanned spruce domestic sales in the same period is [CONFIDENTIAL TEXT DELETED - PRICE FIGURE] Euros and the average price of domestic sales as a whole is [CONFIDENTIAL TEXT DELETED - PRICE FIGURE] Euros.

2. The inclusion by Customs of administrative, selling and general costs that are not associated with the sale of goods

Ilim Timber is concerned that a number of costs have been included in the cost to make and sell calculation that are not associated with the sale of goods by our client's two plants at Wismar being INT and HWN. Many of these costs are overhead costs that are not attributable to Wismar production and do not reflect the true cost to make and sell products exported to Australia.

The key issue that Customs have not considered is that when Ilim Timber purchased the Wismar plants from [CONFIDENTIAL TEXT DELETED - NAME OF COMPANY] in [CONFIDENTIAL TEXT DELETED - DATE] it did not take over any of the [CONFIDENTIAL TEXT DELETED - DESCRIPTION OF BUSINESS FUNCTIONS] functions of these businesses and these have had to be developed almost 'from scratch' similar to what would be required for a start-up business.

These include as follows:

- a. The inclusion in the CTMS of certain management staff costs [CONFIDENTIAL TEXT DELETED - DETAILS OF THEIR MANAGEMENT STAFF COSTS];
- b. The inclusion in the CTMS of the costs of employing a number of sales personnel who are working on acquiring new business. [CONFIDENTIAL TEXT DELETED - DETAILS OF STAFF ALLOCATION];
- c. Depreciation of [CONFIDENTIAL TEXT DELETED - NATURE OF ASSET] that have no connection to production or individual customer business;
- d. Certain financial costs, [CONFIDENTIAL TEXT DELETED - NATURE OF FINANCIAL COSTS].

This issue was raised by our client at the site visit (as well as a number of times thereafter) and the relevant cost items are listed, under the heading 'Total Cost to Make' in Appendix 4 - Final Amended CTMS to the Visit Report. The removal of these costs would make a significant difference to the CMTS figures of between [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] and [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent. It can also be seen from the CTMS figures that it was precisely when Ilim Timber was [CONFIDENTIAL TEXT DELETED - NATURE OF BUSINESS ACTIVITY] in [CONFIDENTIAL TEXT DELETED - TIME PERIOD] that Customs has found a high dumping margin due to the increased [CONFIDENTIAL TEXT DELETED - NATURE OF COSTS].

It should be noted that the above treatment of costs is also consistent with German accounting standards and accepted by the German tax authority.

3. The non-allowance of the costs of allocation of resorting activities in the accounts of INT

Ilim Timber purchased the HWN and INT timber mills from [CONFIDENTIAL TEXT DELETED – NAME OF COMPANY] in [CONFIDENTIAL TEXT DELETED – DATE]. There is considerable cost sharing that occurs between the two mills.

INT pays HWN a fee for [CONFIDENTIAL TEXT DELETED – NATURE OF COSTS] associated with resorting activities. Resorting timber following sawing is an important function to grade products to determine quality. This is because HWN carries out a significant amount of resorting work for INT because [CONFIDENTIAL TEXT DELETED – OPERATIONAL REASONS]. Therefore, HWN recharges the costs for these activities to INT in order to reflect the true costs incurred by INT.

We attach a spreadsheet **Confidential Attachment 2 - '1007-1106 Apportionment of costs (HWN - INT)'**. This clearly sets out the volumes, in cubic metres, that have been subject to resorting activities and the costs involved. This cost item markedly affects the CTMS. For example, in Q3, INT's costs would increase by [CONFIDENTIAL TEXT DELETED – DOLLAR FIGURE] Euros per unit and HWN's costs would reduce by [CONFIDENTIAL TEXT DELETED – DOLLAR FIGURE] Euros per unit. The large difference in the effect on each entity is due to the fact that INT has much [CONFIDENTIAL TEXT DELETED – DESCRIPTION OF VOLUMES] volumes being processed through its mill.

This cost allocation has been included in Ilim Timber's accounts [CONFIDENTIAL TEXT DELETED – EVENT AND DATE]. Ilim Timber is still in a start-up phase and the cost allocation reflected by these entities could not be made until [CONFIDENTIAL TEXT DELETED – DATE].

At the site visit, Ilim Timber representatives were required to provide an enormous amount of information to Customs and, at the time of the visit, Ilim Timber was not aware of the extent to which these cost allocations may affect the cost of production calculations. Our client drew this to the attention of Customs by email on 24 January 2012. It is unacceptable that Customs have refused to take this important issue into consideration, given that it is estimated that it would reduce the cost to make and sell by more than [CONFIDENTIAL TEXT DELETED – PERCENTAGE FIGURE] percent.

4. The inclusion of 'fall down' timber in calculating export prices for Australia

[CONFIDENTIAL TEXT DELETED – DETAILS OF PRODUCTS EXPORTED TO AUSTRALIA].

MGP10 and MGP12 are structural timbers used in load bearing construction, such as in truss and frame construction.

By contrast F5 is of a significantly inferior quality, which means that it is much less expensive than MGP10 and MGP12. F5 is known as fall down timber and is a by product of producing higher quality timbers such as MGP10 and MGP 12. On average, F5 is [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent [CONFIDENTIAL TEXT DELETED - PRICE DESCRIPTION] than MGP12. For example, 190 x 35 F5 sells for [CONFIDENTIAL TEXT DELETED - PRICE AND CURRENCY] per cubic metre compared with [CONFIDENTIAL TEXT DELETED - PRICE AND CURRENCY] per cubic metre for the same dimensions in MGP12.

Customs has calculated the export price to Australia by using an average cost to make and sell of all grades, principally consisting of the three grades referred to above.

The issue we wish to raise is that, in determining export prices, Customs should have excluded F5 sales because there are no equivalent goods of this nature sold in the German domestic market. Any part of the log that is of F5 quality would be sold as low-value packaging material in Germany.

The net effect of including sales of F5 is that it reduces the export price and, all things being equal, it increases the dumping margin.

We refer to **Confidential Attachment 3 - 'F5 price comparison'** which is attached to this submission. This consists of some information provided by the importer of our client's products, Tilling Timber, which verifies the price differences between these different products. We are instructed that up to [CONFIDENTIAL TEXT DELETED - PERCENTAGE FIGURE] percent of orders placed by Tilling Timber comprise of F5.

Our client requests that Customs forthwith reconsider its preliminary findings based on the issues raised above.

We would be pleased to assist Customs to clarify any matters in considering these issues.

Yours faithfully
GROSS & BECROFT



Dr. Ross Becroft
Principal

Encl.