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13 February 2012

Mr Geoffrey Gleeson
Director, Operations 3
International Trade Remedies Branch
Australian Customs and Border Protection Service
Customs House
5 Constitution Avenue
CANBERRA ACT 2601

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Dear Mr Gleeson

Structural Timber exported from Austria, Canada, Czech Republic, Estonia, Germany, Lithuania, Sweden and the USA – Comments re Stora Enso Austria & Sweden Exporter Visit Report

I refer to the recent release of the Stora Enso Austria and Sweden Exporter Visit Report (the Report), the Applicant¹ companies involved in the above inquiry have reviewed the Preliminary Report.

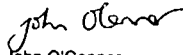
Attached are comments on behalf of the Applicant companies in respect of the nominated Report.

It is understood that the verification of costs is a complex and a time intensive task. In the event you or the Expert consultants require any assistance with the interpretation of the attached document, Mr Tim Sherry of CHH Woodproducts Australia Pty Ltd is available to assist you. Mr Sherry can be contacted on (03) 9258 2600.

The Applicants are reviewing the remainder of the recently released exporter visit reports and will provide comments as soon as practicable. Subject to these reports (and others to be released) the Applicants may comment further on the Stora Enso Lithuania and Stora Enso Austria and Sweden Reports.

If you have any questions concerning this submission please contact me on (07) 3342 1921.

Yours sincerely



John O'Connor
Director

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

¹ Building Supplies Group Holding Pty Ltd, Hyne & Sons Pty Ltd, Gunns Limited.

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Applicants' comments on Stora Enso Austria and Sweden Exporter Visit Report

1.0 Executive Summary

C&BP has preliminarily determined that Stora Enso's exports of structural timber from Austria and Sweden were at non-dumped levels (i.e. minus 9.7 per cent and 9.5 per cent respectively) during the 1 July 2010 to 30 June 2011 investigation period.

The Applicants¹ have reviewed C&BP's Exporter Visit Report for Stora Enso Austria ("SEA") and Stora Enso Sweden ("SES"). It is noted that the SEA Report initially indicated that SEA sold like goods domestically, however, it was subsequently considered this was not the case. The following comments are identified in relation to the issue of 'like goods':

- Claims that construction methods in Austria differ to Australia, and therefore no similar domestic sales to goods exported to Australia (Section 5.4);
- "in many cases" provides little guidance as to whether sufficient domestic volumes were observable (Section 5.5);
- SES has rough sawn timber (dried or undried) domestic sales – specification adjustment can be made based upon verified cost differences between domestic and export sales;
- Claimed by SEA that planed and dried B grade for export only.

Similar to the Applicants submission on the Stora Enso Lithuania ("SEL") Exporter Visit Report, a specification adjustment to goods sold domestically (which are like goods – although not identical) could have been made for domestic sales by SEA.

The Applicants' submit a specification adjustment is possible based upon properly verified CTM&S for the GUC and the domestic selling price(s) for like goods sold by SEA. For instance it was noted in the Report that SEA graded the export material to Australia with the internal grade A specification. This supports the use of the cost differential of grade 0-3 to lesser grades as a basis of a specification adjustment.

In the absence of domestic sales of identical products from another seller on the domestic market in Austria and Sweden, C&BP determined normal values on the basis of Cost To Make and Sell ("CTM&S") under s.269TAC(2)(c) of the Customs Act.

The Applicants have analysed C&BP's documented verification of Stora Enso's Austria and Sweden CTM&S records as detailed in the Exporter Visit Report (i.e. Section 9 of Report). The Applicants hold reservations concerning the following items:

- SE Sweden's claim of not related party purchases, however, the visit report indicates SE Sweden buys from a party which it has ownership;
 - How the profit for logging is accounted for as an internal sale on fibre;
- Absence of benchmarking of log costs (re related party purchases);
- Lack of discussion on log classes used for GUC and linkage back to site and manufacturing yield calculations;
- The absence of the Loss on B Grade product in the CTMS that arises from the production of the GUC;
- No reference to exclusion from log costs of material not involved in production of GUC;
- C&BP appear to have accepted untested SEA's explanation that the log cost for the GUC are below the average timber site cost;
- Fibre and conversion costs description provided insufficient understanding that conversion costs have been correctly associated with fibre (i.e. grossed up for losses through process and reflect actual logs and associated recoveries used rather than site averages for the GUC);

¹ Building Supplies Group Holding Pty Ltd (BSG), Hyne & Sons Pty Ltd, and Gunns Limited.

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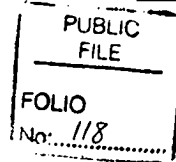
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- Doubt as to whether full S,G&A and finance expenses have been properly identified and included in the GUC and whether an appropriate value for head-office costs have also been included

The SEA & SES Exporter Visit Report appears to have verified the costs allocated on a "whole of site" basis, but has not considered how these costs should be allocated to different products.



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2.0 Global Benchmark Report²

The Global Benchmark Report for 2010 indicates that an equivalent cost estimate in Austria and Sweden for timber ex mill was US\$xxxxx per m³ and US\$xxxxx per m³ respectively on a total site basis (i.e. includes recovery benefit on less processed material). The same report indicated an EBITDA margin being achieved by local mills in addition to costs of US\$xxxxx/m³ for Austria and US\$xxxxx/m³ for Sweden, respectively.

Using the Global Benchmark Report and without making any adjustments for manufacturing process costs associated with the production of MGP, it would be seem unlikely that SEA achieved an MPG cost of \$A xxxxx² (\$USxxxxxx) including profit when fibre alone is estimated to cost \$USxxxx/m³ in the Benchmark Report (*key assumption: xxx% conversion rate*) and the World Resource Quarterly tracked fibre (i.e. spruce) in Austria at a rate (\$USxxx/xxx/xxx m³ in Q3'10/Q4'10/Q1'11 respectively).

The Applicants' modelling suggests MGP production is likely to incur a grade adjustment penalty for SEA using the benchmark report data of at least \$Axxx/m³ in addition to the approx \$xxxm³ whole of site production cost (kiln dried % of production 70%, planed 30%). It is the Applicants' contention that C&BP-verified SEA data understates the ex Mill position for MGP grades exported to Australia.

The same FOB(\$A) value cannot be reliably determined for exports from Sweden due to other exporting entities exporting from Sweden. However preliminary estimates result in a similar understanding and concern regarding the C&BP position on an Ex-Works price for the GUC from SES.

The Applicants believe Expert Review is required to establish the CTMS for the GUC from both SEA and SES.

² Global Timber/Sawmill/Lumber Cost Benchmarking Report .

³ Calculated from ABS weighted average export price for Austria, less local inland freight and dumping margin of minus 9.7 per cent.

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3.0 Cost Modelling – MGP Structural Timber**3.1 Constructed Selling Price - Austria**

A constructed selling price for MGP Grade Structural Timber in Austria based on Global Benchmark Report data is as follows:

(based upon 2010 costs; Average Exchange Rate US\$:A\$ 0.91)

Fibre (\$USxxxxx@ xxx%)	xxxxx	Benchmark rpt – Whole of site avg
Residues (\$US)	(xxxxx)	Benchmark report
Conversion Costs (\$US)	xxxxx	Benchmark rpt – <u>Whole of site avg.</u>
		(Based on KD85%; Planned 60%)
Depreciation (\$US)	xxxxx	Benchmark report
Avg. Moulded Cost (\$US)	xxxxx	Whole of site (Benchmark Report)
MGP Grossed up Conversion adj (\$US)	xxxxx	Modelling for mfr'd grade
		(\$Axxxx); maybe higher
MGP Moulded Cost (\$US)	xxxxx	
Implied Customs adjustment	xxxxx	Different to Benchmark ie \$USxxxx-\$xxxx
Ex Works (\$US)	xxxxx	<u>Excludes Corporate charges</u>
Ex Works (\$A)	xxxxx	Avg cost adj applied, <u>no interest/profit</u>
Freight to Australia (\$A)	<u>71.00</u>	ABS data
	xxxxx	
Duty 5% (\$A)	xxxxx	Based on ABS
On Wharf (\$A)	xxxxx	
Off Wharf to WHS (\$A)	xxxxx	Modelling
WHS Cost (\$A)	xxxxx	Modelled Minimum
Delivery to Customer (\$A)	xxxxx	Modelled Metro rate
Std Cost before S,G&A, int & profit (\$A)	xxxxx	
SG&A (\$A)	xxxxx	Modelled ex <i>(source)</i> Report
Std Cost before interest (\$A)	xxxxx	<u>No profit assumed domestically</u>

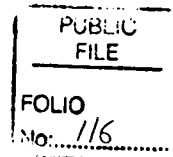
Therefore the calculated conversion cost detailed above in addition to fibre cost is \$Axxxxx/m³ (\$USxxxxx/m³ – i.e. conversion cost + depreciation + MGP Grossed-Up Conversion+ Implied Customs Adjustment).

It is the Applicant's view that SEA does not have an Ex works price including profit, interest charge and loss and the loss on associated B grade product sales of \$Axxxxx/m³ as is suggested by C&BP's finding.

3.2 Conclusions

C&BP's verification is vulnerable in the following key areas:

- (i) Actual fibre cost;
- (ii) Residue costs (i.e. residue credits); and
- (iii) Conversion costs (including yield calculations, allocation of overheads and loss associated with the sale of B Grade product).



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4.0 Comments/Issues with SEA/SES Exporter Visit Report

4.1 *Related party transactions*

The Applicants' maintain similar reservations as expressed in the SEL submission. These concerns are shared equally with the SEA & SES Exporter Visit Report.

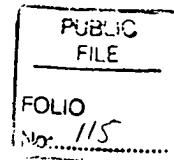
However, the Applicants note that SES has purchased fibre from a "division" of its operation and hence reservations concerning related party transactions are also held.

Stora Enso's adjusted EBIT margin in 2010 was xxx%, therefore will be lower after interest and tax. Were the dumping margin correct, it would suggest that domestic products are being sold at a significant negative margin (which is unlikely since there are multiple players who only sell domestically/close proximity of mill) or that the margin on exports is being significantly overstated.

The location of the meeting and limited representation by mill staff also points to the integrated/related nature of the businesses.

The Applicants assert that the relationships between the related parties will influence the relevant price.

Therefore the concerns of the Applicants in relation to fibre cost and export sales to Australia in respect of related party transaction as highlighted in the SEL response, are also applicable to the SEA and SES Report.



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4.1 Raw Material Costs

The substantiation of the fibre cost is a central element of verification to SEA and SES's CTM&S for the GUC. This area warrants close scrutiny via Expert review.

4.2.1 Material Costs - Fibre

The applicants are hindered from adequately responding to the Report due to an absence of sufficient detail on fibre purchased to produce the GUC:

- C&BP appear to have undertaken limited evaluation of log prices and benchmarking against published indices to establish bona fides of prices in the GUC CTMS
 - There is an absence of any indication that C&BP verified the profile or quality of logs and associated waste process flows used for MGP production;
 - What is the purchased basis of logs; and
 - Associated handling costs through to sawmill.
- There is no discussion in the report on the accounting of profit from forestry activities and its impact on CTM&S calculation:
 - Given the significance of fibre as an input cost, there is a need to look at the market price carefully and comment since the dumping margin estimate suggests prices for fibre well below market as identified in the Application and Global Benchmark report.
- In Austria, log size was briefly discussed (i.e. diameter only), no mention of the whether the log standard is of the grade required for MGP premium product is evident;
- There is limited description of required fibre quality to meet Australian MGP production and availability of sufficient representative log to meet the quantity supplied;
- No calculation appears to have been undertaken that compares the whole-of-site recovery with individual manufacturing yields on domestic products vs export products. This issue needs to be addressed via Expert Review and would leave C&BP better positioned to assess the creditability of the data provided
 - The Report is generally silent on log diameter classes used for the GUC and the comparison to site averages implications of efficiency and yield;
- Income from the sale of the pulp log and roundwood should be removed from the fibre cost of manufacture for structural timber as these products are not associated with structural manufacturing and sell for prices below saw log prices.

Expert assessment is critical to ensure the cost to make was not constructed on a price for non-representative low cost log, size or quality.

4.2.2 Material Costs – Residues

Similar to fibre, residue sales should have been benchmarked to establish the possibility of over-crediting.

- The Report fails to discuss the nature of residue sales and the associated benchmarking and the income earned, thus Expert review is required;
- There is an absence of comment on the exclusion of residue credits for logs chipped or sold by-passing the manufacturing process;
- There is no discussion on the allocating of costs associated with selling the residues that would result in a lower net income as presented;



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- There is an absence of any confirmation of any related activity relying on the consumption of chips and residues outside timber consumption e.g. powerplant.

4.2 Conversion Costs (i.e. sawing, kilning, planing, etc)

The isolation of the costs associated with the GUC should reflect the requirements of the product both in terms of processes and properties.

4.2.1 Process Costs (including Conversion costs)

Sawing

- The Report is silent on the UOM used in the calculation of the CTM&S for SEA (for SES there is limited discussion and the conversion factor is redacted). In the conversion process the reviewer should understand how the recovery through planing has been calculated (i.e. noted the input and output unit of measures, e.g. sawn/nominal/actual cubic metres with each stage of the process).
- Expert Review is required to validate how the cost of the raw material has been grossed up to account for the recovery loss including direct & indirect associated costs;
- The lack of conversation on log class prevents the applicants from commenting on the appropriateness of log recovery/yield ex the sawmill. This requires Expert Review. In particular, this requirement is important in understanding overall site yields.
- Expert Review of conversion costs based on yield from log associated with the production of GUCs is required for contrasting with reported site averages;
 - The Applicants contend as with SEL response that separate to yield, conversion cost penalties from processing smaller log add to significant burden of CTM&S for the GUC. (CHH Confidential Attachment as per submission re SL)
 - Conversion penalty is likely to be up to xx per cent when compared with average costing through the same machine centres.
- The extent to which the manufacturing process for GUC results in co-products of low value and a resultant loss on sale of co-product needs to be applied to the raw material costs of the GUC. Whilst this understanding and inclusion of the loss is fundamental, comment by C&BP on its inclusion in the Report is absent and requires Expert Review.

Other Process Costs

- Discussion on allocation of overheads to machines centres (ie: from start or at end) is absent from the report and should be subject to Expert Review. For instance,
 - In SEA there is no discussion on the treatment of end-trimming;
 - Generally no discussion of packaging costs for export sale to Australia is evident.
- As stated above, the lack of a manufacturing yield calculated for MGP and compared back to whole of site is a significant omission in the verification process.
 - Grade loss – The Applicants based their submission on the knowledge that SEA and SES achieve a xxxx grade outturn based on fibre quality available to them. However the grading standards associated with the GUC will result in greater grade loss than would be normal for domestic product. This grade loss needs to be specifically accounted for in the evaluation of the GUC and reinforces the need for end-to-end product cost as opposed to working site averages;
 - Does a small log provide sufficient fibre for the quantity of GUC supplied to Australia – this includes an assessment of any wide board GUC product (ie> 120mm) from this mill. If not, costings will need to be adjusted further for higher priced fibre in the end-to-end product cost;

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- The Report remains silent on maintenance costs, adequacy and the extent of provisions/capitalising. Expert Review is required to assess the adequacy of the maintenance charges used in the CTMS and linkage to yield and processing cost.
- There is no discussion on the extent of external sawn procurement and associated costs of handling in CTM&S;
- The Report provides an insufficient understanding as to the extent of value-adding process such finger-jointing and their associated placement in the manufacturing process to be able to review and adequately comment on the process and therefore should be subject to further Expert review.
 - FJ and Solid MGP needed to be costed separately as the FJ material incurs significant additional cost post the planing of solid timber that needs to be recovered through selling prices both ex Mill and in Australia – costs substantially higher than the magnitude of the un-dumped margin calculation of C&BP.

4.3 Delivery costs - Freight ex Mill

- It is noted there appears to be no reference to demurrage costs incurred on Australian destined orders being allocated back to the CTMS.
- The report remains silent on the adequacy of any information associated with the dispatch costs incurred in the mill for export sale. A failure to visit the plant may result in lack of clear understanding on the process cost provided.

4.4 Administrative & Other Manufacturing Costs

The Applicants are concerned about:

- The extent to which SG&A costs are being allocated between domestic and export sales, when it is claimed that Austria and Sweden are export focused (i.e. majority of SG&A costs should be allocated to export sales)
 - For example the depreciation may be reported correctly in total, but its allocation to the production centres grossed up for processing loss through the process remains unclear.
- How SE's central Sales & Marketing function is reflected in the CTM&S the GUC needs to be considered in Expert Review?
- Lack of discussion on re Interest and treatment of working capital funding in the CTMS.

4.5 Profit

- Dumping margins calculated suggest only minimal profit assessed in MGP, whereas the benchmark report suggests domestic producers in Austria making xx% and xx% in Sweden for the CY2010 – however C&BP appears have applied a margin of less than xx%.

4.6 Domestic Selling Prices Ex-mill

- The average price approach based on actual sales suggests lack of critical analysis to identify products identified as unprofitable to the mill, and then being made profitable in a subsequent period, possibly at a lower price. As prices fell over the investigation period it would be unlikely that SEA and SES go from being unprofitable from one day to profitable the next;
- It is unclear from Report whether question put about any other Stora Enso entity providing support to Stora Enso Australia.

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- Sales of **B grade** (export reject material) in Australia by Stora Enso are at prices substantially below that achieved on MGP10 or better rated production. The differential gap on in-market selling prices exceeds the noted preliminary un-dumped margin.
- Sales of F5 graded structural material in Australia by Stora Enso are at prices substantially below that achieved on MGP10 or better rated production. The differential gap on in-market selling prices exceeds the noted preliminary un-dumped margin.
- Sales of finger-joint structural studs in Australia by Stora Enso are commonly at the prevailing prices achieved on solid MGP10 rated production and do not reflect the sizeable additional costs incurred in their manufacture.

4.7 Other general concerns:

- The visit was conducted in Austria therefore removing the opportunity for C&BP to independently verify staff numbers, operating modes, asset age and integrity, at Brand and Gruvon. This lack of first hand exposure fundamentally limits C&BP's ability to 'test' the basis of cost allocations for the respective business entities;
- Units of measure (UOM) at each stage of process are not easily identifiable or absent. This creates the opportunity for incorrect calculations. The UOM should be detailed at each step of process.
- The actual exchange rates used to convert back to AUD across the investigation period are omitted;
- Other common production costs may include costs that relate specifically to the MGP GUC, and if included in a "common" category and allocated across all site production, will result in a lowering of the CTM&S for the MGP GUC.

5.0 Conclusions

The SEA/SES Exporter Visit Report is absent on detail as to the extent to which production costs by stage have been verified and 'tested' by C&BP. The absence of detail on log size and quality, yield, etc prevents the Applicants from adequately commenting on the Report. Expert Review is required to express views on the adequacy of cost identification and associated allocations provided for by the exporter, and verified by C&BP.

The Report indicates that the Brand (Austria) and Gruvon (Sweden) Mills were verified for the purposes of the verification visit. The Report is silent as to whether the costs/selling prices for the remaining mills in Austria and Sweden are representative of the verified mills.

The Report indicates that the inefficient and costly Kopparfors mill did export the GUC to Australia in the period under investigation. However it remains silent on how the losses associated with production in producing GUC exported to Australia have been treated.

The Applicants note that following the receipt of Exporter Questionnaire responses, C&BP advised exporters that average costing for the GUC would not be accepted. Whilst it is evident that SEA & SES revised CTM&S information for the GUC, the Applicants have formed the view from the examination of SEA/SES Exporter Visit Report that the verified CTM&S for the GUC remains understated. The Applicants anticipate that the Expert Review enable a fair assessment as to whether costs for the MGP GUC have been appropriately allocated.