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21 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 EESTI Napi (Estonia) Exporter Visit Report

I refer to the Stora Enso EESTI Napi (Estonia) Exporter Visit Report recently placed on the electronic Public File.

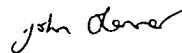
The Applicants have reviewed the SE Napi report. The attached submission addresses the Applicants' concerns following the review of the report.

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 submissions, the Applicants may comment further on matters that may arise in remaining Exporter Visit reports to be reviewed.

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

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Applicants' comments on Stora Enso EESTI AS (NAPI) Exporter Visit Report

1.0 Executive Summary

C&BP has preliminarily determined that Stora Enso's exports of structural timber from its Napi production facility in Estonia were at non-dumped levels (i.e. minus 7.5 per cent) during the 1 July 2010 to 30 June 2011 investigation period.

The Applicants¹ have reviewed C&BP's Exporter Visit Report for Stora Enso EESTI Napi. It is noted that the SE Napi Report has determined normal values on a constructed costs methodology.

The Applicants have analysed C&BP's documented verification of Stora Enso's Napi CTM&S records as detailed in the Exporter Visit Report (i.e. Section 8 of Report). The Applicants hold reservations concerning the following items:

- Stora Enso Napi would appear to purchase significant volumes of sawn timber from a related party – Stora Enso Wood Supply;
- C&BP was satisfied that a comparison of pricing for purchases from Stora Enso Wood Supply demonstrated that the purchases could be considered "arms length". To test this claim C&BP requested an income statement for Stora Enso Wood Supply for the 2010 year
 - The Applicants do not consider this is sufficient evidence to rely upon that timber sales by the entity Stora Enso Wood Supply could be deemed to be arms length;
 - The applicants believe a more robust position would have been to seek evidence as to the purchase price for comparable logs suitable for the GUC (from unrelated Stora Enso Wood Supply entities) and assess whether the subsequent process of sawing is recovered in the Stora Enso Wood Supply selling price to Stora Enso Napi;
- The SE Napi report contains no reference to exclusion from log costs of material not involved in production of GUC;
- The SE Napi report contains no reference to log merchandising activities and associated costs for the GUC;
- There is an absence of discussion of the verification of fibre (quality and size class) and conversion costs (including planing and grading), thus preventing proper analysis to confirm that conversion costs have been correctly associated with fibre (i.e. grossed up for losses through process and reflect actual sawn timber and associated recoveries used rather than site averages for the GUC);
- The SE Napi report contains no review of the costs associated with the treated product;
- The absence of the accounting for the loss on reject/A+B ungraded product in the GUC CTM&S;
- Absence of discussion on the adequacy of maintenance, packaging and dispatch costs incurred in the mill;
- The allocation of the S,G&A and head office costs on basis of total sales, with no attempt to allocate costs on activities associated between domestic and export sales functions;
- No finance charges have been identified.

The Stora Enso Napi Exporter Visit Report appears to have verified the costs allocated on a "whole of site" basis within process, but has not considered how these costs should be allocated to different products.

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

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2.0 Comments/Issues with Stora Enso Napi Exporter Visit Report

2.1 Related party transactions

As per earlier submissions concerning verification of Stora Enso European facilities, the Applicants' have reservations concerning related party transactions. In the Stora Enso Napi report it is apparent that the entity is supplied with logs by the related party Stora Enso Wood Supply.

The Report indicates that Stora Enso Napi purchases logs from related and unrelated parties. Importantly, however, it is stated at Section 8.1.1:

"Stora Enso Napi advised that the Stora Enso Wood Supply undertakes all private log and pulp purchases on behalf of the various mills in Estonia. Stora Enso Wood Supply arranges for the payment, storage and delivery of the log to the Napi mill."

The Applicants' strongly challenge C&BP's conclusion that purchases by Stora Enso Napi from its related supplier Stora Enso Wood Supply can be considered arms' length transactions. These concerns are amplified when it is considered:

- Stora Enso Wood Supply arranges all purchases for Stora Enso mills (including Napi) in Estonia;
- Stora Enso Wood Supply arranges for the **payment, storage and delivery** of the log for Stora Enso Napi
 - C&BP verified "additional" invoices for the "services" undertaken by Stora Enso Wood Supply;
 - It is not clear whether the said "services" relates to the selling functions (including storage & delivery) only;
 - The related party supply arrangements provide no confidence that C&BP verified all costs associated with log supply;
- The payment for the logs by Stora Enso Wood Supply must be questioned as to whether it reflects all costs incurred – particularly where delivery costs have been paid on logs that are supplied from plantations on a stumpage basis only (it is not evident that C&BP verified freight costs incurred by Stora Enso Wood Supply on stumpage sales); and
- The Report documents extended credit terms between SEE and SEA which is inconsistent with international timber trading.

The Applicants assert that the relationship between Stora Enso Wood Supply and Stora Enso Napi warrants further scrutiny than is apparent in the Report. As Stora Enso Wood Supply is responsible for all log purchases by the Napi mill, it is expected that the relationship will affect the price between the parties. C&BP has, for example, identified one instance of separate invoicing for services provided. The Applicants do not consider that C&BP could be adequately satisfied of all costs incurred by Stora Enso Wood Supply having been included in the "services" invoice (i.e. including expenses such as freight for logs purchased on a stumpage basis).

The Applicants maintain concerns that the selling price for log purchases by Stora Enso Napi from its related entity Stora Enso Wood Supply (that arranges payment, storage and delivery of logs) can be accepted as arms length transactions. Independent Expert Review of the verified information, along with forensic analysis that all costs have been accounted for by Stora Enso Wood Supply is warranted.

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4.1 Raw Material Costs

The substantiation of the fibre cost is a central element of verification for structural timber production (both domestic and export sales). The following factors require further analysis via Expert review.

4.2.1 Material Costs - Fibre

The applicants note that Stora Enso Napi purchases logs and sawn timber from related and non-related suppliers. It is evident that C&BP has sought to understand the process and account for the various cost allocations. There are, however, unanswered issues requiring further investigation by the Experts, including:

- C&BP appear to have accepted average costs for all grades produced by Stora Enso Napi. C&BP appear to have accepted unchallenged Stora Enso Napi's explanation on the yield for the GUC.
 - 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 reference to log merchandising activities and associated costs for the GUC;
 - There is an absence of discussion into the verification of fibre quality and size class required for the GUC and compared to site averages;
 - No discussion on treatment of additional costs for logs purchased on a stumpage basis (as opposed to delivered to mill); and
 - The Applicants challenge the premise that higher production yields are possible where tighter properties are required.
- C&BP has undertaken limited evaluation of log prices and benchmarking against published indices to establish bona fides of prices in the GUC CTM&S
 - There is an absence of any indication that C&BP verified market prices based on the required profile or quality of logs used for MGP production;
 - What is the purchased basis of logs; and
 - Associated handling costs through to sawmill.
 - Significant reservations remain concerning the verified cost for the logs and sawn timber purchased by Stora Enso Napi from its related party Stora Enso Wood Supply as noted earlier in the discussion of related parties;
- Stora Enso Napi is purchasing a proportion of their finished fibre as saw timber. The diagram on P. 22 indicated that this saw timber goes into the planing mill without further sawing or drying. There are several issues:
 - Did C&BP check the differences between purchased sawn timber and own manufacture and understand any differences in the cost?
 - Were the sawn timber purchases of the same precise dimensions as to have the same yield loss through the planing mill?
 - How does Stora Enso Napi manage the sawn timber input? Is it on an order by order basis or is it a managed regular volume that would imply a deeper relationship between buyer and seller?
- While C&BP has ensured that the unit cost at each stage reflect the actual volume processed, it is not evident that the sawing cost has been grossed up to allow for the drying and planing losses;
- There is no discussion in the report on the accounting of profit from forestry activities and its impact on CTM&S calculation:

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- 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.
- No independent calculation appears to have been undertaken that compares the whole-of-site recovery with individual manufacturing yields on domestic, other export products and the GUC. 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.

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 & By-products

Similar to fibre, residue and woodchip 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;
- Credits for woodchips have been calculated on a weighted average basis – how does this compare with the World Quarterly Report credits for Estonia?
- There is limited discussion on the allocation of costs associated with selling the residues that would result in a lower net income as presented;
- 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; and
- 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 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 and 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 earlier responses on Stora Enso Reports 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)

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- Conversion penalty is likely to be up to xx per cent when compared with average costing through the same machine centres.
- The Report fails to comment on the yield of downgrade product (i.e. B/reject, A+B or out of specification product) associated with the production of the Australian grade (F5 or better). The sale of downgrade product, whether as a domestic or export sale, results in a loss that must be associated with the GUC CTM&S. Accounting for this loss is **absent** from the Report.

Other Process Costs

- From the Diagram on P.22 of report it appears:
 - Not to appropriately associate maintenance costs in the process of manufacturing sawn timber.
 - Consequently these cost have not been grossed up at the drying and planing stages for loss of volume
 - Is the depreciation cost included in the cost centres and grossed up for yield losses through the production process?
- The proper allocation of overheads incurred in log purchasing and sorting, sawn timber purchasing, waste management from the saw mill etc into the weighted average saw timber cost prior to grossing up for drying and planing losses is an important and correct cost allocation. In the sense that C&BP appear to correctly allocate residues back to saw milling and separately back to planing **but not** fully implemented it in a correct cost allocation
 - After correcting the costing for this error the corrected cost then need to be adjusted for structural grade yield. Both of these adjustments will influence the dumping margins determined.
- Discussion on allocation of overheads to machines centres (i.e.: from start or at end) is absent from the report and should be subject to Expert Review.
- There is an also an absence of discussion in respect of:
 - the treatment of docking and end-trimming;
 - treatment costs (i.e. separate CTM&S for treated GUC, beyond the points of commonality);
 - packaging costs for export sale to Australia.
 -
- 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.
- The Report provides insufficient information on the extent of any value-adding process and 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.

4.3 Delivery costs - Freight ex Mill

- The report remains silent on the adequacy of any information associated with the dispatch costs incurred in the mill for export sale.

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,

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- o 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 of the GUC needs to be considered as part of the Expert Review.
- Lack of discussion on re Interest and treatment of working capital funding in the CTM&S.

4.5 Profit

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

4.6 Domestic Selling Prices Ex-mill

- It is unclear from Report whether question put about any other Stora Enso entity providing support to Stora Enso Australia.
- 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 B/A+B materials in Australia by Stora Enso are commonly at the prevailing prices achieved on solid MGP10 substantially below that achieved on MGP10 or better rated production.

4.7 Other general concerns:

- 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, for example treatment costs for H2 materials.

5.0 Conclusions

The Stora Enso Napi 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 Applicants note that following the receipt of Exporter Questionnaire responses, C&BP advised exporters that average costing for the GUC would not be accepted. The Applicants have formed the view from the examination of Stora Enso Napi's Exporter Visit Report that the verified CTM&S for the GUC remains understated. The Applicants anticipate that the Expert Review will enable a fair assessment as to whether costs for the MGP GUC have been appropriately allocated.

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Key concerns with the Stora Enso Napi Report include:

- Significant further questions about the arm's length relationship with Stora Enso Australia;
- The verification does not discuss log class size and quality, and associated yield for the GUC, contrasted with site averages;
- The report appears to fail in addressing losses on downgrade product (B/reject, A+B, or other out-of-specification products);
- Attempt at full costing does not include the maintenance, depreciation and administration costs shared into the saw mill before grossing up for dryer and planer losses; and
- No apparent adjustment for grade yield due to the higher specification for Australian timber.