



**REPORT TO
THE MINISTER OF FINANCE**

**REQUEST FOR TARIFF RELIEF BY
SEALY CANADA LTD.
REGARDING
CERTAIN WOVEN AND KNITTED FABRICS**

JUNE 28, 1996

SEALY CANADA LTD.

REQUEST NO.: TR-95-056

Request No.: TR-95-056

Tribunal Members: Arthur B. Trudeau, Presiding Member
Desmond Hallissey, Member
Lyle M. Russell, Member

Research Director: Réal Roy

Research Manager: Peter Rakowski

Counsel for the Tribunal: Joël J. Robichaud

Registration and
Distribution Officer: Claudette Friesen

Address all communications to:

The Secretary
Canadian International Trade Tribunal
Standard Life Centre
333 Laurier Avenue West
15th Floor
Ottawa, Ontario
K1A 0G7

INTRODUCTION

On July 14, 1994, the Canadian International Trade Tribunal (the Tribunal) received terms of reference¹ from the Minister of Finance (the Minister) pursuant to section 19 of the *Canadian International Trade Tribunal Act*.² The Minister directed the Tribunal to investigate requests from domestic producers for tariff relief on imported textile inputs for use in their manufacturing operations and to make recommendations in respect of those requests to the Minister.

On October 23, 1995, the Tribunal received a request from Sealy Canada Ltd. (Sealy) of Scarborough, Ontario, for the permanent removal of the customs duty on importations, from all countries, of woven fabrics of textured and non-textured yarns of polyester, polypropylene or rayon; printed warp-knit fabrics of polyester filament yarns; and warp-knit (stitch-bonded) fabrics for use as ticking in the production of mattresses (the subject fabrics).

On January 31, 1996, the Tribunal, being satisfied that the request was properly documented, issued a notice of commencement of investigation, which was widely distributed and published in the February 10, 1996, edition of the Canada Gazette, Part I.³

As part of the investigation, the Tribunal's research staff sent questionnaires to potential producers of identical or substitutable fabrics. Questionnaires were also sent to known and potential users of the subject fabrics for use in the production of mattresses and to several importers of the subject fabrics. A letter was sent to the Department of National Revenue (Revenue Canada) requesting information on the tariff classification of the subject fabrics, and samples were provided for laboratory analysis. Letters were also sent to a number of other government departments requesting information and advice.

A staff investigation report summarizing the information received from these departments, Sealy and other firms that responded to the questionnaires was provided to the parties that had filed notices of appearance for this investigation.

A public hearing was not held for this investigation.

PRODUCT INFORMATION

The textile inputs covered by this request are woven fabrics of textured and non-textured yarns of polyester, polypropylene or rayon; printed warp-knit fabrics of polyester filament yarns; and warp-knit (stitch-bonded) fabrics for use as ticking in the production of mattresses. The subject fabrics are used on the outside of the mattress or foundation. They are quilted to polyurethane rolls, and a panel is cut to the required size. The panel is flanged to an inner spring, together with other filling materials. This procedure is followed for both sides of the mattress.

-
1. On March 20, 1996, the Minister of Finance revised the terms of reference.
 2. R.S.C. 1985, c.47 (4th Supp.).
 3. Vol. 130, No. 6 at 485.

Revenue Canada advised the Tribunal that the subject fabrics are classified under classification Nos. 3921.19.90.00, 5407.73.00.21, 5407.94.00.91, 5516.23.00.90 and 6002.43.90.23 of Schedule I to the *Customs Tariff*.⁴

REPRESENTATIONS

In its request, Sealy alleged that the subject fabrics could not be sourced from Canadian manufacturers. It further indicated that, in 1998, when the U.S. tariff rate on mattresses imported from the United States is scheduled to be eliminated, it will face significant import competition from U.S. manufacturers. Sealy claimed that it requires significant tariff relief in order to remain competitive with U.S. manufacturers that produce mattresses in a substantially lower-cost environment. If tariff relief is granted, Sealy foresees benefits in terms of increased employment, investment and sales volumes, and lower prices and/or better quality for Canadian mattress consumers.

All other mattress manufacturers⁵ that responded to the Tribunal's questionnaire supported the request for tariff relief.

All known potential manufacturers of fabrics identical to or substitutable for the subject fabrics were sent a notice of the Tribunal's investigation and a questionnaire.

Although it produces identical or substitutable fabrics, Rayonese Textile Inc. (Rayonese) supports the request for tariff relief on imports of the subject fabrics. It does not oppose the request because it, along with its U.S. parent company, takes the broader corporate view that the removal of the tariff will be an incentive to further rationalize production and increase efficiency in the Canadian operation.

Two domestic textile manufacturers opposed the request, Rentex Mills Inc.⁶ (Rentex), which claimed to be capable of producing identical or substitutable fabrics, and Doubletex, a fabric converter.

Rentex opposes the request for tariff relief because it claims that it has both the facilities and the knowledge to produce identical or substitutable fabrics. It indicated that, due to the shrinking market, there are only two warp knitters left in Canada. If tariff relief were granted on the subject fabrics, Rentex maintained that it would be adversely affected and claimed that the loss of this market segment would erode its prospects for the future.

Doubletex opposes the request for tariff relief unless it is confined to yarn-dyed woven fabrics of polypropylene and rayon. Furthermore, it indicated that any tariff relief should also contain a provision to permit the duty-free importation of greige fabrics by converting mills.

4. R.S.C. 1985, c. 41 (3rd Supp.).

5. Simmons Canada Inc., Rest-Well Mattress Company Ltd., Waterloo Bedding Co. Ltd., Western Sleep Products Ltd. and Serta Mattress Company.

6. The Tribunal received a questionnaire response from Rentex on May 14, 1996, after the issuance of the staff investigation report and the filing of Sealy's final submission.

The Canadian Textiles Institute (CTI) was of the view that the Tribunal's notice of commencement of investigation expanded the range of fabrics beyond that on which Sealy requested tariff relief. The CTI noted that there were several discrepancies in the tariff classification claimed by Sealy and that indicated in the Tribunal's notice. It also pointed to three companies⁷ that have identified themselves as currently producing and selling, or capable of producing, identical or substitutable fabrics for use in the manufacture of mattresses. In addition, it maintained that, because identical or substitutable fabrics are produced in Canada, domestic manufacturers would not benefit from reciprocal treatment in the U.S. market if tariff relief were granted. According to the CTI, if tariff relief is to be pursued, it should be on a bilateral basis through the *North American Free Trade Agreement*⁸ (NAFTA) acceleration process.

In response to the written submissions of other parties, Sealy emphasized the strong industry support from Canadian manufacturers of mattresses and noted that these companies agree with Sealy's position that ticking of the type used in their production of mattresses is not available from any Canadian source. Sealy also indicated that two of the companies that claimed to produce mattress ticking for the Canadian market were unknown to Sealy and that they did not provide any pertinent information to the Tribunal. Furthermore, the only company, Rayonese, which might be considered capable of producing mattress ticking, fully supports the request for tariff relief.

Sealy also stated that, although it imports all or most of its mattress ticking from the United States, it is considering importing from non-NAFTA sources. For this reason, it has asked that tariffs applicable to mattress ticking from the United States and all other countries benefiting from the MFN tariff be removed. This would strengthen the competitive position of the industry and, since there is no evidence of domestic production of mattress ticking, should not cause any harm to the Canadian textile industry. Furthermore, it is claimed that granting tariff relief in respect of imports from one country and refusing to grant similar relief in respect of imports from other countries, when the basis for such relief is the absence of actual or potential production of identical or substitutable fabrics, would violate the fundamental principle of contracting parties embodied in "Article I of the GATT (General Most-Favoured Nation Treatment)."

In response to the CTI's submission that there is confusion with respect to the tariff classification of the subject fabrics, Sealy agrees with Revenue Canada's tariff classification and, therefore, there should be no further confusion in this respect. Regarding the CTI's point that tariff relief should be pursued on a bilateral basis through the NAFTA acceleration process, Sealy submits that the reciprocal treatment for Canadian producers in export markets is outside the Tribunal's mandate. Sealy also questioned the relevance of this point, since there is little or no evidence of Canadian production of mattress ticking.

Sealy also stated that, as there is no Canadian production of identical or substitutable fabrics, the only cost of the requested tariff relief is the net cost of the foregone revenue to the federal government.⁹ This cost,

7. Rentex, LaGran Canada Inc. and Rayonese.

8. Done at Ottawa, Ontario, December 11 and 17, 1992, at Mexico, D.F., on December 14 and 17, 1992, and at Washington, D.C., on December 8 and 17, 1992 (in force for Canada on January 1, 1994).

9. According to Sealy, the net cost to the federal government will be the uncollected tariffs, offset by any income taxes collected from the domestic manufacturers of mattresses, if the tariff relief is not passed on directly to consumers. Sealy also notes that the terms of reference do not require the Tribunal to consider uncollected tariffs and that the Tribunal has not rejected any request for tariff relief simply on this basis.

according to Sealy, will be outweighed by the benefits to Canadian mattress manufacturers and to Rayonese, all of which support the request. Finally, Sealy requested that the tariff on the subject fabrics from all countries be permanently removed as of the date of the filing of its request, that is, October 23, 1995.

The Department of Industry (Industry Canada) indicated that Sealy now sources the majority of its fabrics from the United States and that it is benefiting from declining NAFTA rates, which will reach zero on January 1, 1998. Industry Canada further indicated that, in the event that Sealy proposes to import fabrics from non-NAFTA sources, it will benefit from declining textile tariffs in accordance with the lower textile tariffs recommended in 1990 by the Tribunal, which were lowered further in the recently concluded Multilateral Trade Negotiations. Industry Canada's submission also referred to the "yarn-forward" and "fabric-forward" rules which require that the production of some of Sealy's textile inputs, as well as the manufacturing of end products, take place in North America.

The Department of Foreign Affairs and International Trade informed the Tribunal that the Government of Canada does not maintain quota restraints on fabrics classified under classification No. 3921.19.90.00, 5516.23.00.90 or 6002.43.90.23, with the result that these fabrics are not subject to any quantitative import restrictions. However, Canada currently maintains quota restraints on polyester filament fabric, including any fabric mixed mainly or solely with polyester filaments imported from Poland, the Republic of Korea and Taiwan. This coverage includes the subject fabrics classified under classification Nos. 5407.73.00.21 and 5407.94.00.91. Bilateral agreements, which provide for these restrictions, between the Government of Canada and the Government of the Republic of Korea and the Taiwan Textile Federation have been in place since 1978. Quota limits on polyester fabrics were implemented to protect Canadian manufacturers from large volumes and low prices of exports from these countries.

ANALYSIS

The Minister's terms of reference direct the Tribunal to assess the economic impact on domestic textile and downstream producers of reducing or removing a tariff and, in so doing, to take into account all relevant factors, including the substitutability of imported textile inputs with domestic textile inputs, the ability of Canadian textile producers to serve the Canadian downstream industries and a domestic versus foreign price comparison. In determining whether or not to recommend tariff relief, a key consideration for the Tribunal is the extent to which tariff removal will provide net economic gains for Canada.

Although the request for tariff relief is supported by all domestic mattress manufacturers, as well as by a large textile manufacturer, it is opposed by two domestic textile manufacturers, Rentex and Doubletex.

Rentex is a privately owned company which manufactures warp-knit fabrics for the apparel, sportswear, automotive, home furnishings and medical sectors. In its questionnaire response, Rentex argued that, although it has not produced an identical fabric, it has the facilities to provide Sealy with a 100 percent polyester version of the printed warp-knit fabric. However, the questionnaire response provided no quantitative information that would further assist the Tribunal, nor did Rentex submit any samples or evidence of plans to produce identical or substitutable fabrics in the near future. In previous cases, the Tribunal has stated that it requires more than assertions of the ability to supply identical or substitutable fabrics. It also requires evidence that a producer has furnished domestic users with identical or substitutable fabrics or that it is in the process of establishing the supply of identical or substitutable fabrics for domestic users. Further, domestic textile producers should be able to demonstrate their ability and willingness to

supply both large and small quantities of identical or substitutable fabrics on acceptable commercial terms.¹⁰ In this respect, Rentex has not demonstrated to the Tribunal that it can supply identical or substitutable fabrics.

Doubletex opposes the request for tariff relief unless it is confined to yarn-dyed woven fabrics of polypropylene and rayon, and it has requested that any tariff relief also contain a provision to permit the duty-free importation of greige fabrics by converting mills. However, Doubletex did not provide any technical or sales information with respect to the polyester/cotton woven fabrics which it allegedly sells to mattress manufacturers. Consequently, the Tribunal was not able to conclude that Doubletex produces identical or substitutable fabrics or determine the economic impact of granting tariff relief.

Finally, the only textile manufacturer which appears to be able to supply identical or substitutable fabrics, Rayonese, supports the request for tariff relief. Consequently, the Tribunal concludes that no domestic production would be affected by removing the duty on the subject fabrics.

In the staff investigation report, the Tribunal's staff estimated that the removal of the tariff on the subject fabrics would result in significant savings for the domestic industry. Furthermore, Sealy indicated in its request that tariff relief would help it remain competitive and foresaw benefits in terms of increased employment, investment and sales volumes and lower prices and/or better quality for Canadian mattress consumers. Other mattress manufacturers concurred with Sealy's assessment of the benefits of tariff removal.

Given that the removal of the tariff would have a positive impact on the competitiveness of Sealy and other mattress manufacturers in the domestic market, and considering that the granting of tariff relief would provide net economic gains for Canada, the Tribunal recommends that tariff relief be granted on an indeterminate basis.

With respect to the CTI's position that any tariff relief should be confined to imports from NAFTA sources, the Tribunal accepts Sealy's argument that it may want to import from MFN countries in the future. In any event, this point is irrelevant since imports from non-NAFTA countries cannot cause any damage when there is no Canadian production of identical or substitutable fabrics.

With respect to CTI's argument that, if tariff relief is to be pursued, it should be on a bilateral basis through the NAFTA acceleration process, the Tribunal has indicated in a previous report¹¹ that this issue is clearly outside the Tribunal's mandate.

10. See Report to the Minister of Finance: Requests for Tariff Relief by Château Stores of Canada Ltd. and Hemisphere Productions Inc. Regarding Armani Gabardine, Request Nos. TR-94-011 and TR-94-019, September 19, 1995; Report to the Minister of Finance: Request for Tariff Relief by Peerless Clothing Inc. Regarding Woven Fabrics of Flax, Request No. TR-94-012, January 17, 1996; and Report to the Minister of Finance: Request for Tariff Relief by Palliser Furniture Ltd. Regarding Certain Woven Rubber Webbing, Request No. TR-94-010, August 23, 1995.

11. See Report to the Minister of Finance: Request for Tariff Relief by Palliser Furniture Ltd. Regarding Woven Cut Warp Pile Fabrics, Request No. TR-95-014, May 1, 1996.

While the Tribunal recognizes the potential danger of creating a tariff anomaly regarding imported greige fabrics that may be identical to or substitutable for the subject fabrics, it finds that it is inappropriate to make a recommendation that is wider than the scope of the investigation.

With regard to Sealy's request for retroactive tariff relief, the Tribunal does not believe that there are any extraordinary competitive circumstances that warrant such a recommendation.

RECOMMENDATION

In view of the above information and evidence submitted to the Tribunal in this matter, the Tribunal hereby recommends to the Minister that all customs duties on importations from all countries of:

woven fabrics of textured and non-textured yarns of polyester, polypropylene or rayon;
printed warp-knit fabrics of polyester filament yarns; and warp-knit (stitch-bonded) fabrics
classified under classification Nos. 3921.19.90.00, 5407.73.00.21, 5407.94.00.91,
5516.23.00.90 and 6002.43.90.23 for use as ticking in the production of mattresses

be removed for an indeterminate period of time.

Should the Minister grant tariff relief pursuant to the Tribunal's recommendation and a Canadian producer commences production of identical or substitutable fabrics, that producer may request the commencement of an investigation for the purpose of recommending an amendment to the order of the Governor in Council that provided tariff relief.

Arthur B. Trudeau
Arthur B. Trudeau
Presiding Member

Desmond Hallissey
Desmond Hallissey
Member

Lyle M. Russell
Lyle M. Russell
Member