

REPORT TO THE MINISTER OF FINANCE

**REQUEST FOR TARIFF RELIEF BY
LENROD INDUSTRIES LTD.
REGARDING
CERTAIN NONWOVENS**

NOVEMBER 10, 1998

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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 with respect to those requests to the Minister.

On February 13, 1996, Lenrod Industries Ltd. (Lenrod) of Saint-Laurent, Quebec, made a request (Request No. TR-95-066) to the Tribunal for tariff relief on imports, from Denmark, of nonwovens, consisting of polypropylene staple fibres mixed solely with polyester staple fibres, thermally bonded on one side and thermally bonded or thermally embossed on the other side, for use in the manufacture of furniture, mattresses and mattress supports.

On February 25, 1997, after conducting an investigation of Lenrod's request, the Tribunal issued a report to the Minister in which it recommended that tariff relief not be granted at that time. In its report, the Tribunal noted the following:

Under the present circumstances, the Tribunal must be concerned with the ability of the furniture and bedding industries to have established and competitive sources of the subject fabrics or any substitutable fabrics in order to sustain their competitive position vis-à-vis imports of the finished products. Although domestic producers of allegedly substitutable fabrics, notably Texel, seem to have the ability to respond to the needs of users, failure to do so would, in the Tribunal's view, prejudice the position of the furniture and bedding industries in the market. The Tribunal is of the view that, if domestic producers do not demonstrate their capability to produce and sell identical or substitutable fabrics to these industries at competitive prices in a reasonable time period, say, 12 months, then it would be open to Lenrod to file a new request with the Tribunal.³

On February 27, 1998, the Tribunal received a new request from Lenrod seeking the removal, for an indeterminate period of time, of the customs duty on imports of the same nonwovens as those covered in its request of February 13, 1996 (the subject nonwovens).

On June 3, 1998, the Tribunal, being satisfied that the request was properly documented, issued a notice of commencement of investigation which was distributed and published in the June 13, 1998, edition of the *Canada Gazette*, Part I.⁴

As part of the investigation, the Tribunal's research staff sent questionnaires to potential producers of the subject nonwovens and of identical or substitutable nonwovens. Questionnaires were also sent to a number of potential importers of the subject nonwovens.

1. On March 20 and July 24, 1996, and on November 26, 1997, the Minister of Finance revised the terms of reference.

2. R.S.C. 1985, c. 47 (4th Supp.).

3. *Report to the Minister of Finance: Request for Tariff Relief by Lenrod Industries Ltd. Regarding Nonwoven Fabrics*, Request No. TR-95-066, February 25, 1997, at 10.

4. Vol. 132, No. 24 at 1317.

The Department of National Revenue (Revenue Canada), having already provided its advice as to the tariff classification of the subject nonwovens in 1996, was not asked to carry out another laboratory analysis. However, the Department of Foreign Affairs and International Trade (DFAIT) was asked to provide current information on any quantitative import restrictions on the subject nonwovens, and the Department of Industry and the Department of Finance were informed of the request and asked to provide any relevant comments.

PRODUCT INFORMATION

In the notice of commencement of investigation, the nonwovens were described as consisting of polypropylene staple fibres mixed solely with polyester staple fibres, thermally bonded (area bonded) on one side and thermally bonded or thermally embossed (point bonded) on the other side, to be cut to customers' specific size requirements, then rewound and packaged, for use in the manufacture of furniture, mattresses and mattress supports (box springs).

The subject nonwovens are classified under tariff item No. 5603.93.90 of the *Customs Tariff*,⁵ as indicated to the Tribunal by Revenue Canada at the time of the original request in 1996. The classification number was 5603.93.90.50 in 1997 and is 5603.93.90.40 in 1998. In 1998, nonwovens classified under tariff item No. 5603.93.90 are dutiable at 16 percent *ad valorem* under the MFN tariff and are duty free under the US tariff, the Chile tariff, the Mexico tariff and the Canada-Israel Agreement tariff.

The subject nonwovens are cut by Lenrod to customers' specific size requirements, then rewound and packaged, for use in the manufacture of furniture, mattresses and mattress supports. All production is carried out in one of Lenrod's two facilities in Saint-Laurent: its 40,000-s.q. ft. facility located at 500 Deslauriers Street or its 18,000-sq. ft. facility located at 365 Deslauriers Street.

REPRESENTATIONS

Lenrod employs 42 people, 28 of whom are production personnel. The number of employees engaged directly in the production of the end products produced from the subject nonwovens was not provided. Lenrod is seeking tariff relief because it alleges that identical or substitutable nonwovens are not available domestically.

Lenrod submitted that, while domestic producers are able to produce needle-punched nonwovens, the subject nonwovens are needle-punched thermally bonded or thermally embossed. Lenrod stated that it has expended considerable efforts to identify or develop domestic sources of production of identical or substitutable nonwovens, but with no success. It claimed that there are no domestic producers of identical or substitutable nonwovens.

Lenrod submitted that, after the Tribunal's decision not to recommend tariff relief, it conducted long, but eventually fruitless, discussions with Texel Inc. (Texel) based on the producer's promises to the Tribunal in the original investigation that took place in 1996. In that regard, Lenrod filed a letter from Texel dated May 8, 1997, in which Texel indicated that it did not intend to start production of identical or substitutable nonwovens. Lenrod also filed a letter from Jasztext Fibers Inc. (Jasztext), which stated that Jasztext did not intend to invest in specialized equipment to produce identical or substitutable nonwovens.

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

Lenrod claimed that only Nolar Industries Limited (Nolar) and Montreal Fabrics Corp. Ltd. (Montreal Fabrics) opposed the request despite the fact that neither is a manufacturer of nonwovens. Lenrod stated that, since Nolar is not a producer, it constitutes a third party and that, therefore, its objection should not be considered.

Lenrod submitted that, although Nolar alleges that it is in the process of purchasing an embossing machine, embossing in itself is not a relevant issue because the subject nonwovens are thermally bonded and that the embossing of a thermally bonded nonwoven is a simple operation that is more akin to finishing than manufacture. Lenrod argued that, if the machinery is purchased, Nolar will be embossing imported fabrics, not producing identical or substitutable nonwovens. According to Lenrod, Nolar's plans are "brought out and dusted off" each time that there is a request for tariff relief and its commitment to purchasing an embossing machine is minimal. Lenrod also argued that it is unclear whether the machine that Nolar is planning to purchase is really an embossing machine, since the purchase order offered in evidence does not specify any embossing capabilities.

With regard to Montreal Fabrics, Lenrod argued that there is no support to the claim that the quilted decking that Montreal Fabrics imports and sells is substitutable for the subject nonwovens. Furthermore, no producer of quilted decking has opposed the request.

Lenrod submitted that tariff relief would result in net economic benefits to Canada. Although the staff investigation report estimates benefits to Lenrod as being based on a certain percentage of its imports, Lenrod stated that tariff relief will encourage additional cutting and rewinding in Canada, such that benefits will further increase. Lenrod further stated that, with tariff relief, it would import a considerably greater percentage of the subject nonwovens in a form required for cutting and rewinding, which will substantially increase total duty savings per annum. According to Lenrod, these savings would benefit end users and, therefore, tariff relief could only result in net economic benefits to Canada.

According to Lenrod, Nolar's claim that tariff relief will result in it losing a major proportion of its sales volume "should be disregarded as totally unreliable." Lenrod argued that any lost sales to Nolar resulting from tariff relief would affect only US producers, since there are no Canadian producers and that, should Nolar lose sales, these sales will be gained by a Canadian converter such as Lenrod. Thus, submitted Lenrod, the net economic effect to Canada of Nolar's lost sales, if there were to be any, is nil.

Domestic Producer of Nonwovens

Texel, of Saint-Elzéar, Quebec, was the only domestic producer of nonwovens to respond to the Tribunal's notice of commencement of investigation. Texel stated that it did not oppose Lenrod's request, but expressed concern that the broad range of nonwovens covered by tariff item No. 5603.93.90 could open the door to imports of nonwovens classified under the same tariff item as the subject nonwovens, but used for other end uses. It cautioned the Tribunal, if recommending tariff relief, to ensure the use of a classification number specific to the nonwovens for which tariff relief has been requested.

Domestic Users of Nonwovens

Simmons Canada Inc. (Simmons), of Mississauga, Ontario, is a domestic manufacturer of mattresses and mattress supports. Simmons fully supported the removal of the customs duty on the subject nonwovens. It makes significant use of "cut-to-size" nonwovens in its manufacturing operations and, to its

knowledge, nonwovens manufactured to the specifications that it requires are not available from any Canadian textile manufacturer.

Palliser Furniture Ltd. (Palliser) reiterated its support for the request for tariff relief by Lenrod, as it had done in the Tribunal's previous investigation in 1996. Palliser stated that tariff relief on other textile inputs had helped it compete against imports in Canada and improved its competitive position in the United States. It noted, in particular, that its leather upholstery plants had experienced rapid expansion due, in part, to tariff relief.

Domestic Producer of Allegedly Identical or Substitutable Nonwovens

Nolar, which has been in business since 1974, employs 16 people in its plant in Concord, Ontario. Five employees are directly involved in the production of cut-to-size nonwovens that Nolar claims are substitutable for the subject nonwovens and intended for the same end uses.

Nolar opposed the request for tariff relief on two grounds: (a) it claims to be a competitor of Lenrod's selling substitutable nonwovens; and (b) it claims to have made plans to purchase the equipment to produce embossed nonwovens. Nolar stated that, as a converter of nonwovens which sells products that are substitutable for and identical to the subject nonwovens, there is no discernible difference between the operations and services that it provides to its customers and the operations and services that are provided by Lenrod. Nolar also opposed the request because it claims to have been on the verge of purchasing, in June 1998, the required embossing equipment to consolidate the manufacture of the relevant products in its facilities in Concord, Ontario. Nolar claimed that the present investigation has delayed this planned purchase, however, and that granting the tariff relief requested would eliminate Nolar's incentive to proceed with this purchase.

According to Nolar, tariff relief would favour the products of companies which import from MFN countries at the expense of its own products which use inputs from NAFTA countries (Canada, the United States and Mexico).

Nolar submitted that the support given to Lenrod in 1996 by Simmons and Palliser was greatly exaggerated and is no longer valid. Nolar further submitted that there are no facts to support that tariff relief would increase the production and exports of these two companies. Instead, Nolar argued that these companies would be unaffected by tariff relief.

Other Submissions

Montreal Fabrics opposed the current request for tariff relief because it sells materials to Canadian quilters that use them to make quilted decking. It claimed that, as both quilted decking and needle-punched thermally bonded decking are used for the same end use, they are substitutable. Montreal Fabrics argued that, if tariff relief is granted on the subject embossed nonwovens, the quilted decking would be overpriced and that this would result in a loss of jobs in Canada.

Montreal Fabrics also argued that two domestic producers of nonwovens have not completely ruled out their ability to produce the embossed and the box spring filler cloth. In addition, it submitted that another domestic producer was actively working to produce embossed nonwovens and that Montreal Fabrics was in discussion with this company to purchase these nonwovens. Accordingly, Montreal Fabrics argued that there

is no need to eliminate the tariff when, potentially, Canadian firms have the ability to produce such nonwovens.

OTHER INFORMATION

The Tribunal was informed by DFAIT that Canada does not maintain quota restraints on nonwovens classified under tariff item No. 5603.93.90. These nonwovens, therefore, are not subject to any quantitative import restrictions.

Revenue Canada stated in 1996, with respect to the first investigation, that there would be no additional costs, over and above those already incurred by it, to administer the tariff relief requested for the subject nonwovens.

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 doing so, to take into account all relevant factors, including the substitutability of imported textile inputs for domestic textile inputs and the ability of domestic producers to serve the Canadian downstream industries.

This is the second investigation conducted by the Tribunal regarding a request for tariff relief on the subject nonwovens. When, further to its 1996 investigation, it recommended to the Minister that tariff relief not be granted for these nonwovens, the Tribunal stressed that, if domestic producers could not demonstrate, within a one-year period, their capability to produce and sell identical or substitutable nonwovens at competitive prices, it would then be open to Lenrod to file a new request. The evidence indicates that, immediately after the issuance of the Tribunal's recommendation, Lenrod entered into negotiations with Texel, the producer that appeared, in Lenrod's view, the most likely to produce nonwovens acceptable to its applications and the one highlighted in the Tribunal's report to the Minister. However, these negotiations proved unsuccessful, and Texel has now abandoned plans to produce these nonwovens. Consequently, Lenrod filed a new request for tariff relief at the expiry of the one-year period, as suggested by the Tribunal.

This request covers a specific type of nonwovens, namely, needle-punched, thermally bonded nonwovens that can be either plain or embossed. The evidence reveals that this type of nonwoven, either plain or embossed, is not produced in Canada.

As to the distinction between the three types of nonwovens available in the Canadian marketplace and their substitutability, the Tribunal is of the view that neither spunbonded nor needle-bonded nonwovens are substitutable for the subject nonwovens because each type of nonwoven is sold at different price points and for different end uses. The Tribunal notes, in this regard, that no producers of nonwovens of any type filed any submission in opposition to the request. In fact, as for the two domestic producers of nonwovens that intervened during the 1996 investigation to oppose Lenrod's request for tariff relief, Texel indicated in this investigation that it does not oppose the request, while Jasztext did not respond to the Tribunal's notice of commencement of investigation. Furthermore, the Tribunal notes that Veratec Canada Inc., the domestic producer of spunbonded nonwovens that sells to Nolar, did not oppose Lenrod's request.

The two companies that have opposed the request for tariff relief are a converter of nonwovens manufactured by other producers, Nolar, and an importer-wholesaler, Montreal Fabrics.

The evidence shows that Nolar currently sources needle-punched thermally bonded nonwovens equivalent to the subject nonwovens in the United States. It cuts and finishes these nonwovens to customers' specifications. The operations performed by Nolar are virtually identical to Lenrod's, except that the latter's imports are from Denmark at a 16 percent MFN rate of duty, while Nolar's imports qualify as goods of US origin and are, thus, duty free.

Nolar estimated that granting tariff relief to Lenrod would result in a loss to Nolar of a substantial percentage of its sales volume of substitutable nonwovens. The number of employees involved in the production of these nonwovens would decrease substantially, as would the number of hours worked annually. On the other hand, if tariff relief is not granted, Nolar claims that it will invest in embossing/perforating equipment and provide a number of additional jobs for Canadians.

The Tribunal is not persuaded by Nolar's arguments. Nolar is currently operating as a direct competitor to Lenrod, while benefiting from a significant advantage in customs duties (zero versus 16 percent). The Tribunal notes that all recent tariff agreements involving Mexico, Chile and Israel⁶ provide for duty-free imports of the subject nonwovens. Removing the MFN tariff on these products would level the playing field for all market players. While Nolar may have to reduce its prices of substitutable nonwovens as a result of tariff relief, the Tribunal does not believe that it will have the dire consequences predicted by Nolar.

With regard to Nolar's plans to purchase new embossing equipment and its assessment that the equipment would result in cost savings that would be passed on to furniture manufacturers, as well as enhance Nolar's ability to export to the United States, thus creating new jobs, the Tribunal is concerned that it took Nolar so long to find this equipment and that it could only be found after Lenrod filed a second request for tariff relief on the subject nonwovens. The Tribunal notes that this equipment does not produce nonwovens, but is only capable of embossing nonwovens sourced, at least for the foreseeable future, outside Canada and that Nolar has provided no evidence as to the type of cost savings or export opportunities that this equipment will provide.

Finally, with regard to Montreal Fabrics' opposition to tariff relief because it sells fabrics to Canadian quilters that use it to make quilted decking, the Tribunal notes that there is no indication on the file, other than Montreal Fabrics' allegations, that quilted decking competes with the subject nonwovens, that there were no submissions filed by quilters for or against tariff relief and that Montreal Fabrics did not provide any information relating to the projected losses in sales volumes or values that it would incur if the request for tariff relief were to be granted.

The information presented indicates that tariff relief would provide benefits to Lenrod in excess of \$100,000 per annum. Tariff relief would also provide a benefit to domestic manufacturers in the furniture and bedding industries in the form of reduced costs, thereby enhancing the competitiveness of these industries and allowing their members to compete more effectively in the Canadian and US markets.

In summary, the Tribunal finds that the tariff relief requested by Lenrod would provide net economic gains to Canada.

6. The Mexico tariff with regard to Mexico, the Chile tariff in the case of Chile and the Canada-Israel Agreement tariff in the case of Israel.

RECOMMENDATION

The Tribunal recommends to the Minister that tariff relief be granted, for an indeterminate period of time, on importations from all countries of nonwovens consisting of polypropylene staple fibres mixed solely with polyester staple fibres, thermally bonded (area bonded) on one side and thermally bonded or thermally embossed (point bonded) on the other side, to be cut to customers' specific size requirements, then rewound and packaged, of subheading No. 5603.93, for use in the manufacture of furniture, mattresses and mattress supports (box springs).

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