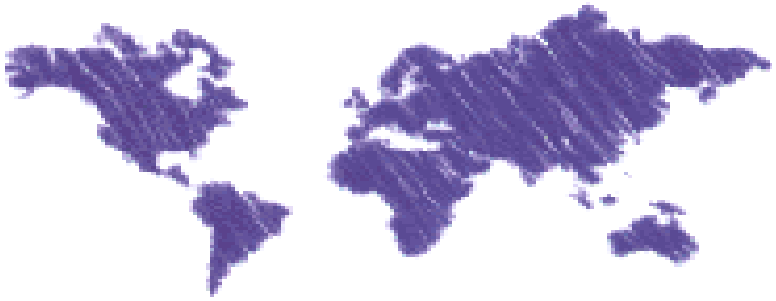
SUBSIDIES ENFORCEMENT ANNUAL REPORT TO THE CONGRESS



Joint Report of the
Office of the United States Trade Representative
and the U.S. Department of Commerce
February 2003

Table of Contents

EXECUTIVE SUMMARY

As part of the U.S. government's commitment to the vigorous enforcement of trade agreements and to ensuring our trading partners' adherence to the terms of those agreements, the Office of the U.S. Trade Representative (USTR) and the Department of Commerce (Commerce) have continued their close collaboration to monitor and strictly enforce the obligations of the Agreement on Subsidies and Countervailing Measures (Subsidies Agreement, or Agreement). The Subsidies Agreement, which establishes multilateral disciplines on subsidies, is the primary instrument for reining in the use of distortive subsidy practices worldwide. The United States pursues enforcement of its rights under the Subsidies Agreement through its participation in the World Trade Organization's (WTO) Subsidies Committee, bilateral contacts, multilateral pressure and, where justified, WTO dispute settlement proceedings. The basic goal of these activities is to deter distortive subsidization and prevent or remedy harm caused to U.S. producers and workers as a result of such subsidies by foreign governments. By working actively to address some of the most important causes of unfair trade distortions, the subsidies enforcement program is helping to strengthen the open, competitive trading environment that is of enormous benefit to American producers and consumers alike.

Doha Development Agenda

In the coming year, the Administration will continue to take strong, proactive steps to address the impact of distortive subsidies on American firms and their workers in both the United States and foreign markets. To accomplish this, the Administration will continue pushing its affirmative agenda in the WTO rules negotiations and will pursue the negotiating objectives set forth in the Trade Act of 2002 to strengthen the international subsidy discipline regime. The existing WTO disciplines on subsidies, while substantial, prohibit only a narrow range of subsidy practices. Permitted subsidies can also distort markets, and therefore, need to be addressed. In this regard, the negotiating mandate agreed to at the Fourth Ministerial Conference – which launched a new round of global trade negotiations, known as the Doha Development Agenda (DDA) – is critically important because it provides an avenue to deal with these other practices and to inform the discussions of subsidy and antidumping measures in a constructive manner. Equally important, the negotiating mandate permits the United States to include in its affirmative agenda proposals that will defend the legitimate interests of U.S. exporters, who are increasingly subject to unfair trade cases abroad.

The Ministerial negotiating mandate also included the initiation of negotiations aimed at eliminating harmful fish subsidies. The United States has believed for some time that the depleted state of the world's fisheries is a major economic and environmental concern, and that subsidies contribute to overcapacity and have substantial trade-distorting effects. Negotiations in this area provide an important opportunity to advance simultaneously trade liberalization, environmental protection, and development goals. It is for these reasons that the United States has played a very active role in these negotiations and will continue to do so throughout the coming year.

Steel

The Administration has also continued to aggressively pursue its agenda, as framed by the President's 2001 Initiative on Steel, to address the structural problems of the global steel industry that have contributed to a decades-long, cyclical proliferation of unfair trade competition and trade remedy responses. An unprecedented series of discussions at the Organization for Economic Cooperation and Development (OECD) among the world's major steel-producing countries led this past year to a consensus that government subsidization has been one of the most significant factors contributing to the historical excess of inefficient steelmaking capacity worldwide.[1] In December, the OECD process culminated in a landmark decision by the participating countries to begin work on the elements of an agreement for reducing or eliminating trade-distorting subsidies in steel, with a view towards incorporating the results of this work into the WTO. The United States actively contributed to the analysis and led the deliberations which produced this outcome, and will approach the follow-on work with similar commitment and determination. Moreover, the negotiating mandate to clarify and improve existing subsidy disciplines, agreed upon at the WTO's Fourth Ministerial Conference, affords the United States the opportunity to eventually integrate this part of the Administration's initiative into the WTO. This will allow us to effectively address the long term market-distorting practices that have historically and intractably plagued the global steel industry and international steel trade.

WTO Subsidies Committee

This past year also marks an important step in addressing some of the practical concerns expressed by many developing countries regarding the implementation of their commitments under the WTO Subsidies Agreement. Specifically, all developing countries, with the exception of lesser developed countries listed in Annex VII of the Agreement, were to eliminate their industrial export subsidy programs by the end of 2002. However, the Subsidies Agreement allows for extensions of this obligation to be given to developing countries under certain circumstances. In addition, special procedures for extensions were agreed to during the Fourth Ministerial Conference for small exporter developing countries. Throughout the process of reviewing the extension requests made in 2002, the United States took a leadership role in the WTO Subsidies Committee to define as narrowly as possible the scope of the extensions – being mindful of concerns U.S. industries may have with these extensions – while also seeking to address legitimate developing country concerns. This exercise exemplifies the broader U.S. approach of pragmatically addressing developing country implementation issues.

---

[1] The countries participating included: Argentina, Australia, Austria, Belgium, Brazil, Bulgaria, Canada, China, Czech Republic, Denmark, Egypt, European Commission, Finland, France, Germany, Greece, Hungary, India, Italy, Japan, Korea, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Romania, Russian Federation, Slovak Republic, Spain, Sweden, Switzerland, Chinese Taipei, Turkey, Ukraine, the United Kingdom and the United States.

China

Another significant development, and one with important implications for subsidies and trade remedy-related monitoring and enforcement, was that 2002 marked China's first full year of membership in the WTO as well as the inaugural year of the Transitional Review Mechanism (TRM) instituted in connection with China's accession. In accordance with the terms of China's protocol of accession, the TRM is a special multilateral procedure used to assess the extent and quality of China's compliance with its WTO obligations on an annual basis for the first eight years of China's membership, culminating in a final review by the tenth year. Reviews are to take place before a number of councils and committees, including the Subsidies Committee. The first review in the Subsidies Committee took place this past November, and the United States was an active participant in seeking clarification from China regarding its efforts to comply with WTO subsidy-related rules and disciplines. In this first critical year of China's accession to the WTO, we have also been closely monitoring and analyzing its subsidy programs and economic policies, and have extended or offered various types of technical training opportunities in order to assist the Chinese in meeting their WTO commitments. This is an area where considerable time and resources will continue to be devoted throughout the coming year. Overall, while China still needs to provide further information about its subsidy programs and pricing policies, China's first review under the TRM in the subsidies area did generate needed clarifications and a constructive review of China's new countervailing duty regulations.

Conclusion

As we move forward with a strong affirmative agenda in the WTO, we will continue our monitoring, counseling and advocacy activities designed to serve the interests of those U.S. parties facing particular problems from subsidized competition. The fundamental aim of these activities is not to generate trade disputes or to punish or retaliate against subsidization, *per se*. While the United States will not shrink from exercising its internationally recognized rights to offset the effects of injurious, subsidized imports into the U.S. market, our underlying objective is to seek ways of addressing such problems without imposing yet more costs and obstacles to international commerce and investment. Thus, the objective of the subsidies enforcement program is to provide a proactive tool to identify and root out subsidization that is demonstrably distortive of competition and the efficient allocation of economic resources. By addressing the problem of unfair subsidies at their source, whether through advocacy, negotiation or legal action, the Administration seeks to free efficient U.S. firms and workers from the burden of having to compete with foreign treasuries, to free U.S. taxpayers from the consequences of political pressure to compete with such subsidization, and to offer U.S. consumers and citizens the full range of choice, quality and affordable prices that can only be obtained through engagement in a dynamic and competitive global economy.

INTRODUCTION

U.S. trade policy responses to the problems associated with foreign subsidized competition provide USTR and Commerce with both unique and complementary roles. In general, it is USTR's role to coordinate the development and implementation of overall U.S. trade policy with respect to subsidy matters, represent the United States in the World Trade Organization (WTO), including its Subsidies Committee, and chair the interagency process on matters of policy. The role of Commerce, through Import Administration (IA), is to enforce the countervailing duty (CVD) law and to provide the technical expertise needed to analyze and understand the impact of foreign subsidies on U.S. commerce. USTR and Commerce also work closely with, and receive valuable input and advice from, other federal agencies represented in the Trade Policy Staff Committee – such as the Departments of State, Treasury and Agriculture, and Council of Economic Advisors – concerning the full range of issues pertaining to the obligations of our trading partners under the Subsidies Agreement.

With the enactment of the Uruguay Round Agreements Act (URAA) in 1994, the two agencies' roles were further articulated and mutually reinforced in order to facilitate the exercise of U.S. multilateral rights with respect to subsidies that harm the interests of U.S. firms and workers. Among the joint responsibilities assigned to USTR and Commerce, as set forth in section 281(f)(4) of the URAA, is the submission of an annual report to the Congress describing the Administration's monitoring and enforcement activities throughout the previous year. This report constitutes the eighth annual report to be transmitted to the Congress pursuant to this provision.

MULTILATERAL NEGOTIATIONS

A. WTO NEGOTIATIONS

1. Ministerial Declaration

In November 2001, a new round of global trade negotiations – known as the Doha Development Agenda (DDA) – was launched at the Fourth Ministerial Conference. In the Ministerial declaration, the United States secured a two-stage mandate to improve the disciplines under the Subsidies and Antidumping (AD) Agreements and address the trade-distorting practices that give rise to CVD and AD duties. The initial issue identification phase is expected to continue at least up until the Cancun Ministerial Conference in September 2003. Critically, the mandate recognizes that the negotiations must preserve the basic concepts, principles and effectiveness of the two Agreements and that unfair trade laws are legitimate tools for addressing unfair trade practices that cause injury. Under this mandate, the United States has pursued an aggressive, affirmative agenda, aimed at strengthening the rules and addressing the underlying causes of unfair trade practices.

The existing WTO disciplines on subsidies prohibit only two types of subsidies: subsidies contingent on export performance ("export subsidies") and subsidies based on the

use of domestic over imported goods ("import substitution subsidies"). Other permitted subsidies, however, also distort markets and international trade patterns. The specific language of the mandate agreed to at the Fourth Ministerial Conference is particularly important because it provides an avenue to address these other practices and to inform the discussions of subsidy and AD measures in a constructive manner. Moreover, it provides an avenue to address the Trade Promotion Authority (TPA) negotiating objectives and other subsidy concerns in key sectors of the U.S. economy.

The negotiating mandate has also permitted the United States to include in its affirmative agenda proposals that will defend the legitimate interests of U.S. exporters, who are increasingly becoming subject to unfair trade cases abroad. As discussed below, in 2002, the United States submitted a paper to the Rules Negotiating Group identifying issues in this area and laying the groundwork for clarifying and strengthening the rules on trade remedy procedures to ensure that the practices of other countries are as transparent and fair as those in the United States. This will enable U.S. exporters to compete abroad with the assurance that they will not be denied fundamental procedural due process protections.

An important accomplishment of the United States at the Fourth Ministerial Conference was the inclusion of fish subsidies as part of the rules negotiations. The United States has believed for some time that the depleted state of the world's fisheries is a major economic and environmental concern, and that subsidies that contribute to overcapacity and overfishing, or have other trade-distorting effects, are a significant part of the problem. The inclusion of fishery subsidies in the rules negotiations represents a significant opportunity for all countries to advance simultaneously the goals of trade liberalization, environmental protection, and economic development.

2. Progress to Date

a. General

The Rules Negotiating Group held five formal meetings in 2002, under the Chairmanship of Ambassador Tim Groser from New Zealand. Discussions in the Group to date have been based on submitted proposals in the following three areas: (1) AD; (2) subsidies, including fisheries subsidies; and (3) regional trade agreements. Because the Group has been in the initial issue identification phase of the discussions, most of the papers formally submitted by Members have raised issues for discussion rather than specific proposals to change the agreements, with some of the papers presenting questions or comments on prior submissions.

Given the Doha mandate that the basic concepts and principles underlying the AD and Subsidies Agreements must be preserved, the United States presented a paper at the October 2002 meeting outlining the basic concepts and principles of the trade remedy rules. The U.S. paper identified four core principles which will guide U.S. proposals for the Rules Negotiating Group:

- First, it is essential that the negotiations be designed to maintain the strength and effectiveness of the trade remedy laws, and complement a fully effective dispute settlement system which enjoys the confidence of all Members.

- Second, trade remedy laws must operate in an open and transparent manner – thus, the existing transparency and due process obligations need to be refined.

- Third, disciplines must be enhanced to address more effectively underlying trade-distorting practices. Work has already begun along these lines with respect to the steel sector in discussions at the OECD – the United States intends to build on those efforts in the context of the rules negotiations.

- Fourth, it is essential that dispute settlement panels and the Appellate Body, in interpreting obligations related to trade remedy laws, follow the appropriate standard of review and do not impose on national authorities obligations that are not contained in the Agreements.

In furtherance of these principles, the United States presented two papers. The first paper was a submission made by the United States in the context of the OECD High Level Process on Steel. It was submitted to the Rules Negotiating Group for informational purposes, as a concrete illustration of how market-distorting practices could be addressed in a variety of sectors. In order to correct or guard against the full gamut of the distortions in the steel sector, the paper emphasizes the need to reach beyond "classical" subsidies. In broad terms, the paper highlights the goal of the elimination or restriction of as many distortive practices as possible so that market forces – not government intervention – become the main determinants of economic activity in the steel industry. In presenting the paper to the Rules Negotiating Group, it was emphasized that the far-reaching approach advocated for the steel sector was an important and useful guide for the work in the Rules Negotiating Group.

The second paper focused on improving the investigatory procedures in AD and CVD investigations, highlighting a number of areas in which interested parties and the public could benefit from greater openness and transparency by investigating authorities, as well as some areas where improved procedures could reduce costs. As noted above, because U.S. exporters have been a major target of foreign AD and CVD proceedings, it is essential to improve transparency and due process to ensure the fair treatment of U.S. export interests.

b. Subsidies

In the subsidies area specifically, the United States submitted a paper on special and differential treatment at the November 2002 meeting. The purpose of the paper was to: (1) review the generally accepted view on the trade-distorting nature of subsidies; (2) outline the perspective of the United States generally on the issue of special and differential treatment; and (3) highlight the substantial and existing special and differential provisions of the

Subsidies Agreement, as well as the significant practical implementation problems addressed in the lead-up to and at the Fourth Ministerial Conference at Doha.

As to the trade-distorting nature of subsidies, the U.S. paper discussed the longstanding and widespread agreement that subsidies distort market signals which, in turn, undermine the efficient allocation and utilization of resources. This results in oversupply by inefficient producers on the one hand and the closure of otherwise efficient and competitive facilities on the other, resulting in costly budgetary outlays, inefficient use of resources and distortions in international trade flows.

While recognizing the integral role that special and differential treatment plays in the WTO system, the U.S. submission notes that the Subsidies Agreement envisions that, over time, all countries will be subject to a single set of disciplines and that the special and differential treatment provisions were not intended to be in effect in perpetuity. The submission makes clear the U.S. view that the Subsidies Agreement does not endorse indiscriminate subsidization policies as an effective, permanent economic development tool or that it is necessary to expand the special and differential treatment provisions of the Subsidies Agreement to allow greater undisciplined subsidization on the part of developing and lesser-developed countries. Rather, the special and differential provisions of the Subsidies Agreement should be seen as temporary deviations from the normal disciplines necessary to promote trade liberalization and growth, which should only be invoked to the extent necessary and consistent with an individual country's particular economic, financial and development needs.

Lastly, the U.S. submission makes the point that the existing, substantial special and differential treatment provisions of the Subsidies Agreement – found in Article 27 – have been commended as a rational approach to the issue of special and differential treatment for developing and lesser-developed countries in the rules-based trading system of the WTO. In particular, the use of the per capita income threshold in Annex VII of the Subsidies Agreement, has been referred to as a sensible and objective basis for identification of those poorer developing countries in need of particular assistance and an appropriate mechanism to provide a temporary respite from fulfilling the normal rules.[2] Further, the Subsidies Agreement recognizes that once a developing or lesser-developed country becomes export competitive in a product area, it is no longer in need of special and differential treatment.

In conclusion, the U.S. submission – noting the importance of the special and differential treatment issue – proposed that: (1) the WTO Secretariat survey the literature on the topic of subsidies and special and differential treatment and make available to all Members the important academic work that has been done in this area; and, (2) a substantial portion of the agenda for at least one meeting of the Rules Negotiating Group early next year be devoted to a discussion of the special and differential provisions in the Subsidies Agreement.

---

[2] *Trade, Development and the WTO: A Handbook*, World Bank, 2002, pg. 507.

Other submissions on subsidy issues have been made by Brazil, Canada, the European Union (EU), India and Venezuela. Among the issues raised in these papers are: proposals for additional special and differential treatment provisions; the OECD Arrangement on export credits; numerous subsidy calculation methodology issues; the need to re-examine the original framework of the Subsidies Agreement (*i.e.,* the traffic light approach to the categorization of subsidies), including a possible greenlight category for certain types of subsidies provided by developing countries; "disguised subsidies" (*i.e.*, subsidies ostensibly of a general nature but intended to benefit a specific company or industry); import substitution subsidies; and subsidies provided through state-owned or -controlled entities. It should also be noted that many of the issues raised in the AD context, especially in regard to procedural and injury issues, are equally applicable in the CVD area.

In 2003, the United States will make additional submissions on subsidy issues to the Rules Negotiating Group. These contributions will be aimed at ensuring that the work mandated by Ministers remains focused on strengthening the existing disciplines set forth in the Agreement.

c. Fisheries Subsidies

At Doha, the Ministers committed to negotiations that "aim to clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries." The decision to take up fisheries subsidies represented an important milestone for the WTO: for the first time, concerns for environmental conservation and sustainable development – not only traditional trade concerns – were an important issue in the launch of a trade negotiation. This is in large part due to broad support these negotiations enjoy, not only from the United States and other developed countries such as New Zealand and Iceland, but also from a large number of developing countries (a reflection of the critical role the fisheries sector plays in supplying food and a source of livelihood for their people). However, a limited number of other key WTO members, notably Japan and Korea, have opposed the negotiations moving forward by questioning the link between subsidies and overfishing.

The Subsidies Agreement already prohibits certain subsidies (particularly those directly designed to promote exports) and establishes some controls over most others. However, the existing rules are designed primarily to address traditional types of market distortions, such as price depression and loss of market share. The current rules were not designed to address directly the impact of subsidies that contribute to the actual *depletion* of the resource and consequent denial of access to producers from other countries.

The discussion during the initial phase of the negotiations to date has focused on the question of whether fisheries subsidies have, in fact, led to environmentally harmful overfishing, and whether fisheries subsidies pose particularly unique problems which justify a stronger and/or separate set of rules. In two papers submitted thus far, the United States, joined by a number of developed and developing countries (including Australia, Chile,

Ecuador, Iceland, New Zealand, Peru, and the Philippines), has argued forcefully in favor of the important benefits that stronger disciplines on fisheries subsidies would have for trade, development and the environment. On the opposite side, Japan and Korea, in particular, have made submissions arguing that inadequate fishery management, rather than fisheries subsidies, are the cause of the present poor state of the world's fisheries. Mindful of U.S. industry and environmental issues, the United States intends to continue playing a leading role as these negotiations progress into the next phase of identifying the possible structure and content of new fisheries subsidy disciplines.

d. Agreement on Agriculture

At the Fourth WTO Ministerial, WTO Members agreed to an ambitious mandate for agriculture, including "substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support." The United States has taken the lead in calling for substantial reform of agricultural trade policies, across all countries and all products. The United States has proposed comprehensive reform by reducing high levels of allowed protection and trade-distorting support through formulas that reduce tariff and subsidy disparities across countries, as well as strengthening WTO rules on a range of trade-related measures.

The current WTO Agreement on Agriculture places limits on the use of export subsidies. The United States has proposed phasing out the allowed use of export subsidies over a five year period. The goal of eliminating export subsidies in these negotiations is supported by many WTO Members, in particular developing countries. Specific proposals have also been submitted for reforming other export-related government programs, including export credits, food aid, and privileges enjoyed by state trading enterprises. Several Members have also proposed stronger rules to discipline the use of export restrictions.

While governments may provide domestic support to farmers, the Agreement on Agriculture encourages that such support be given in a manner that causes no or minimal distortions to production and trade. Moreover, the Agreement on Agriculture caps trade-distorting domestic support that a Member can provide to its farmers, but preserves the criteria-based "green box" policies that can provide support to agriculture in a manner that minimizes distortions to trade.

The United States has proposed a reduction in the level of trade-distorting support and the establishment of a ceiling on all trade-distorting support that applies equally to all countries. Under the U.S. proposal, the ceiling would be set at five percent of the value of total agricultural production. This proposal, when phased in over five years, would cut the amount of global allowed trade-distorting support by over $100 billion a year, reducing unfair competition in world markets and eliminating disparities resulting from unequal levels of support provided in the base period. Some WTO Members have called for the elimination of all trade-distorting support, and while others have called for strengthening disciplines, or imposing a cap on the green box of non-trade-distorting support.

With respect to market access, the WTO Agreement on Agriculture required the conversion of non-tariff barriers, such as quotas and import bans, into simple tariffs. The United States has proposed substantial reductions of all tariffs through the use of a tariff reduction formula that would bring all tariffs down in a manner that results in all countries having similar tariff levels.

For 2003, the Doha mandate identifies two key deadlines for the agriculture negotiations. First, "modalities", such as tariff and subsidy reduction formulas, are to be established by March 31, 2003. Second, based on these modalities, WTO Members are to submit initial draft schedules of specific commitments, such as reduction schedules for individual tariff lines and subsidy allowances, by the Fifth Ministerial Conference in Cancun.

e. Dispute Settlement Understanding

The current system of dispute settlement at the WTO is an outgrowth of Members' experiences with the weak dispute settlement mechanism that existed under the General Agreement on Tariffs and Trade (GATT), where parties could delay the dispute settlement process and easily block the adoption of GATT panel reports. Because of U.S. frustration with the GATT dispute settlement system, Congress identified as a principal negotiating objective during the Uruguay Round the creation of a dispute settlement system that provided for more effective and expeditious dispute resolution. Such a system was achieved during the Uruguay Round and the resulting Dispute Settlement Understanding (DSU) that was adopted by the WTO Members now governs the conduct of disputes in the WTO.

During the Uruguay Round, Members mandated that there be a review of the DSU within five years to consider Members' experiences under the new dispute settlement system and whether there was a need for further refinements and improvements to the agreement. Although such a review began within the five years mandated by the Members, the work was not completed at the time of the Fourth Ministerial Conference. Consequently, the Ministers at Doha mandated negotiations on improvements and clarifications of the DSU, based on the work that had been done thus far, as well as any additional proposals by Members, with the aim of completing the negotiations by May 2003.

These negotiations are currently underway, and the United States is taking an active role in them, guided by its experiences as both a complainant and a respondent in WTO disputes. Overall, the United States has generally fared well in WTO dispute settlement, particularly as a complainant. The United States has used WTO dispute settlement to open markets for U.S. business; to ensure that U.S. workers can compete fairly; to eliminate trade-distorting practices from the global marketplace; and to defend U.S. laws and policies.

Nevertheless, the United States is concerned with the approach that dispute settlement panels and the WTO Appellate Body have taken in certain disputes and the potential systemic implications it may have. In particular, the Administration believes that, at times, panels and the Appellate Body have improperly applied the applicable standard of

review, particularly in disputes involving U.S. trade remedies, including CVD measures, and have imposed obligations and restrictions on the United States and other Members that are not supported by the text of the WTO agreements.

Congress, sharing such concerns, provided in section 2105 of the Trade Act of 2002 that the Secretary of Commerce transmit to Congress a report setting forth the executive branch's negotiating strategy for addressing these concerns. On December 30, 2002, the Secretary of Commerce transmitted this report to Congress, outlining the executive branch's strategy and the proposals the United States has tabled thus far to achieve its negotiating goals. These proposals would provide greater flexibility and Member control in the dispute settlement process, including the ability to more effectively address errant panel reasoning, that should help avoid erroneous and unnecessary findings in future dispute settlement procedures. They would also increase the transparency of the dispute settlement process, based on the belief that a dispute settlement system that is more open to, and better understood by, the public will have greater public support. The report also notes that in the context of the Rules negotiations, the United States will promote the proper application of the standard of review and the recognition that dispute settlement panels and the Appellate Body are not to impose obligations or restrictions on Members that are not in the text of the Rules agreements. Through this strategy, the United States seeks to improve several aspects of the DSU while maintaining the strength and effectiveness of trade remedies.

f. Going Forward

The work of the Rules Negotiating Group in 2003 will continue to focus on identifying issues at least up through the Fifth Ministerial Conference in Cancun this September. The United States will continue to pursue an aggressive affirmative agenda, based on the TPA negotiating objectives and the four core principles identified in the first U.S. submission discussed above. The United States expects to make a number of written submissions raising numerous other issues to be addressed by the Rules Group, as well as posing additional questions with respect to the submissions made by other Members.

B. STEEL: MULTILATERAL EFFORTS TO ADDRESS MARKET-DISTORTING PRACTICES

Pursuant to the President's Initiative on Steel, announced on June 5, 2001, the United States has been engaged in ongoing efforts over the past year within the framework of the OECD High Level Process on Steel to address overcapacity and market-distorting practices in the global steel sector. High Level delegates have met a total of five times since the process got under way in September 2001, and two subsidiary committees were created in 2002 and tasked with assessing on a more probing basis the respective issues of overcapacity and market-distorting practices. These bodies, known as the Disciplines Study Group and the Capacity Working Group, held two meetings each in 2002.

At the most recent High Level meeting, in December 2002, participating delegations took stock of the work completed by the subsidiary bodies and agreed on a package of follow-on steps. With respect to disciplining market-distorting practices, participants decided to begin work immediately to develop the elements of an agreement for reducing or eliminating trade-distorting subsidies in steel. In addition, they agreed to explore undertaking a voluntary commitment to refrain from introducing new subsidy programs that may maintain or enhance steel capacity. Moreover, where practicable and without compromising the priority work on subsidies, they indicated that they might pursue efforts at a later stage to address other distortions in the global steel market. It was determined that the work on subsidies should proceed on an expedited basis in the Disciplines Study Group, and be concluded in 2003, with consideration to be given to how the results of this work should be integrated into the WTO framework. The Administration looks forward to contributing actively to this work, as we view it as a landmark opportunity to deal seriously and comprehensively with one of the principal causes of the structural capacity imbalances and recurring trade frictions that have afflicted the global steel industry over the past 40 years.

Regarding efforts to evaluate progress in reducing excess capacity, the High Level Process initiated in 2002 a rigorous semi-annual peer review system in which participants submit and review data on the current status of their respective steel industries, including information on the closure of steel capacity. At its December 2002 meeting, the High Level Group identified 140 million tons of capacity that could be closed during the period 1998 through 2005, based on present market conditions. In addition to adopting improvements in reporting and review procedures that should enable participants to obtain a better understanding of current conditions in the global steel market, the Capacity Working Group will also evaluate the feasibility of options for assisting steel plant closures. While the feasibility study of options to facilitate plant closure is intended to be completed this year, the peer review process for tracking industry restructuring will continue beyond 2003 so long as participants consider it useful.

Throughout 2002, the United States actively participated in the OECD exercise and engaged its trading partners with the express objective of ensuring that these multilateral efforts contribute meaningfully to the President's plan to seek reductions in inefficient, excess steelmaking capacity worldwide and to eliminate market-distorting practices which help to sustain such capacity. In September, we were the only participant to table a paper outlining a series of bold proposals aimed at tackling a broad range of distortive practices in the steel sector. Our recommendations to substantially prohibit all distortive steel subsidies were endorsed by a broad range of international steel industry associations. We worked closely with our North American Free Trade Agreement (NAFTA) partners to strive for and signal publicly the kind of market-opening results we expected from the OECD process, and to announce a plan to pursue such goals immediately within the North American market. We coordinated with the EU to promote a broad, common vision for moving forward with an aggressive subsidies reform agenda for steel and to cooperate on ways to encourage continued restructuring and adjustment internationally. We also reached out to China and other critical participants to urge their continued participation in and commitment to this

important work. The United States will continue in 2003 to press ahead with these efforts as we seek to eradicate inappropriate government intervention and other distortions from the international steel market.

MONITORING AND ENFORCEMENT

The Subsidies Agreement establishes multilateral disciplines on subsidies and provides mechanisms for challenging government programs that violate these disciplines. In addition to setting forth rules and procedures to govern the application of CVD measures by WTO Members with respect to injurious, subsidized imports, the Subsidies Agreement also contains disciplines to address the impact of subsidies on trade in foreign markets. These disciplines are enforceable through binding dispute settlement, which specifies strict time lines for bringing an offending practice into conformity with the pertinent obligation. The remedies in such circumstances can include the withdrawal or modification of a subsidy program, or the elimination of the subsidy's adverse effects.

The Agreement nominally divides subsidy practices among three classes: prohibited (red light) subsidies; permitted yet actionable (yellow light) subsidies; and permitted, non-actionable (green light) subsidies. Export subsidies and import substitution subsidies are prohibited. All other subsidies are permitted, yet are also actionable (through CVD or dispute settlement action) if they are (I) "specific", *i.e.*, limited to a firm, industry or group thereof within the territory of a WTO Member and (ii) found to cause adverse trade effects, such as material injury to a domestic industry or serious prejudice to the trade interests of another WTO Member. Although originally three kinds of government assistance qualified as non-actionable, at present the only non-actionable subsidies are those which are not specific, as defined above.[3]

On the basis of these categories of discipline, the Subsidies Agreement provides remedies for subsidies affecting competition in one's domestic market, in the market of the

---

[3] Prior to 2000, Article 8 of the Agreement provided that certain limited kinds of government assistance granted for industrial research and development (R&D), regional development, or environmental compliance purposes would also be treated as a non-actionable subsidy so long as such assistance conformed to the applicable terms and conditions for green light subsidies set forth in Article 8. In addition, Article 6.1 of the Agreement provided that certain other subsidies, referred to as dark amber subsidies, could be presumed to cause serious prejudice. These were: (i) subsidies to cover an industry's operating losses; (ii) repeated subsidies to cover a firm's operating losses; (iii) the direct forgiveness of debt (including grants for debt repayment); and (iv) when the *ad valorem* subsidization of a product exceeds five percent. If such subsidies were challenged on the basis of these dark amber provisions in a WTO dispute settlement proceeding, the subsidizing government would have the burden of showing that serious prejudice had *not* resulted from the subsidy. However, as explained in our 2000 report, a mandatory review was conducted in 1999 under Article 31 of the Agreement to determine whether to extend the application of the green light and dark amber provisions beyond December 31 of that year. Because a consensus could not be reached among WTO Members on whether, or the terms by which, these provisions might be extended beyond their five-year period of provisional application, they expired on January 1, 2000.

subsidizing government and in third country markets. These disciplines serve as an important complement to the U.S. CVD law which is limited to addressing the effects of foreign subsidized competition in the United States. Although the procedures and remedies are different, the Subsidies Agreement provides an alternative tool to address distortive foreign subsidies that affect U.S. businesses and workers in an increasingly global marketplace. Within Commerce, these activities are carried out by IA through the Subsidies Enforcement Office (SEO).

In 2002, the monitoring and enforcement activities of USTR and Commerce fell into the following categories: (1) pursuing and defending U.S. interests in the ongoing work of the Subsidies Committee and the consideration of subsidy-related implementation issues; (2) actively participating in China's Transitional Review Mechanism; (3) examining subsidy-related issues in the WTO accession process and Trade Policy Review of several countries; (4) counseling the U.S. private sector and relevant government agencies about WTO subsidy disciplines; (5) stationing and interacting with overseas Trade Remedy Compliance Staff (TRCS); (6) monitoring foreign subsidy practices and activities; and, (7) taking action to enforce U.S. rights and protect U.S. interests, ranging from WTO dispute settlement to formal and informal advocacy to assist U.S. firms, farmers and workers.

A. WTO SUBSIDIES COMMITTEE

The Subsidies Committee's active agenda in 2002 included ongoing notification and review activities along with extensive discussions throughout the year regarding the export subsidy extension requests made by numerous Members, as well as other residual implementation issues referred to it by the Fourth Ministerial Conference. As in previous years, the United States sought to work pragmatically to address legitimate, practical implementation problems consistent with the policy, practice or legal framework of the United States' subsidy enforcement regime. Beyond participating in the ongoing work of the Committee, the United States: (1) expressed serious concerns regarding government financial assistance provided to the Korean specialty paper industry; (2) actively participated in China's Transitional Review Mechanism; and, (3) joined the consensus in selecting a new Member for the Permanent Group of Experts.[4]

---

[4] Article 24 of the Agreement directs the Committee to establish a Permanent Group of Experts (PGE), "composed of five independent persons, highly qualified in the fields of subsidies and trade relations." The Agreement articulates three possible roles for the PGE: (i) to provide, at the request of a dispute settlement panel, a binding ruling on whether a particular practice brought before that panel constitutes a prohibited subsidy, within the meaning of Article 3 of the Agreement; (ii) to provide, at the request of the Committee, an advisory opinion on the existence and nature of any subsidy; and (iii) to provide, at the request of a WTO Member, a "confidential" advisory opinion on the nature of any subsidy proposed to be introduced or currently maintained by that Member. (To date, the PGE has not yet been called upon to perform any of the aforementioned duties.) Article 24 further provides for the Committee to elect the experts to the PGE, with one of the five experts being replaced every year. At the beginning of 2002, the members of the Permanent Group of Experts were: Prof. Okan Aktan (Turkey); Mr. Jorge Castro Bernieri (Venezuela); Dr. Marco Bronckers (Netherlands); Professor R.G. Flores Junior (Brazil); and Mr. Hyung-Jin Kim (Korea). At its spring 2002 regular meeting, the Committee re-elected Professor Aktan

1. Subsidy Notifications

Subsidy notification and surveillance is one means by which the Subsidies Committee and its Members seek to ensure adherence to the disciplines of the Agreement. In some instances, notification is mandatory, while in others it is an optional feature that can be used to secure a benefit provided by the Agreement – such as to make use of transition periods during which a Member would come into conformity with Agreement norms. In keeping with the objectives and directives expressed in the URAA, and as demonstrated by the extensive use of the SEO's Electronic Subsidies Enforcement Library, WTO subsidy notifications also play an important role in the United States' monitoring and enforcement activities to protect U.S. rights and benefits under the Subsidies Agreement.

Under Article 25.2 of the Agreement, Members are required to report certain information on all measures, practices and activities that, as set forth in Articles 1 and 2 of the Agreement, meet the definition of a subsidy and are specific within the territory of a Member. Under the Agreement, "new and full" notifications are submitted every third year, whereas updating notifications (usually containing information solely on changes made to previously notified subsidies) are submitted in the intervening years. Article 26 of the Agreement charges the Committee with reviewing the full notifications at special sessions held every third year, whereas updates are reviewed at regular, semi-annual Committee meetings.

In 2002, the Committee continued its examination of new and full notifications submitted for 1998 and 2001, as well as updating notifications submitted for 1999 and 2000. The table in Attachment 1 of this report shows the 44 Members (counting the European Union (EU) and its 15 member states as one) whose notifications were reviewed by the Subsidies Committee last year, indicating the annual reporting period to which the reviewed notifications relate.

Importantly, the United States submitted its subsidy notification in 2002. This notification included "updating" notifications for 1999 and 2000, and a "new and full" notification for 2001. Researching and assembling the necessary detailed information regarding U.S. assistance programs and consulting throughout with numerous federal and state agencies was an immense undertaking and commitment of staff and resources for USTR and Commerce. Altogether over 200 federal and state measures were notified to the Subsidies Committee. While certain subsidy information could not be provided – mostly regarding U.S. domestic agricultural supports – the notification filed by the United States in 2002 substantially brought it into compliance with its subsidy notification obligations under the Agreement.

As of January 1, 2002, when Membership in the WTO had reached 144, only 51 Members had submitted new and full subsidy notifications for 2001, while 47 and 39

---

to serve another term.

Members, respectively, had submitted updating notifications for the 1999 and 2000 periods. Notably, 32 Members have never made a subsidy notification to the WTO.

In 2002, the Committee continued to accord special attention to the general matter of subsidy notifications and the process by which such notifications are made to and considered by the Subsidies Committee. In this regard, the Committee took action to address the poor and declining state of compliance with subsidy notifications in an effort to find a long term solution to the problem. The United States' primary goal regarding the notification work of the Subsidies Committee continued to be the full and timely adherence by WTO Members with their subsidy obligations while being open to alternative approaches to lessen the burden of meeting certain notification obligations without diminishing their substance.

In view of the ongoing difficulties experienced by Members in meeting the Agreement's subsidy notification obligations, a three-prong strategy has been employed. The first prong was to examine alternative practical approaches to the frequency and nature of subsidy notifications, as well as their review. In 2001, Members decided to devote maximum effort to submitting new and full notifications every two years, and to de-emphasize the review of the annual updating notifications. Examination of the format for a subsidy notification constitutes the second prong of the strategy. Efforts in this regard were made in 2002 and will continue into 2003. The third prong was the organization of a subsidy notification seminar, geared to participation by capital-based officials responsible for preparing notifications, held prior to the fall committee meeting. (This notification seminar is discussed further in the "Other Technical Assistance" section of this report.)

2. Review of Countervailing Duty Legislation, Regulations and Measures

Throughout the year, WTO Members continued to submit notifications of new or amended CVD legislation and regulations and of CVD investigations initiated and decisions taken. These notifications were reviewed and discussed by the Committee at both of its regular meetings. In reviewing notified CVD legislation and regulations, the Committee procedures provide for the exchange in advance of written questions and answers in order to clarify the operation of the notified measures and their relationship to the obligations of the Agreement. The United States continued to take a leading role in the Committee's examination of the operation of other Members' CVD laws and their consistency with the obligations of the Agreement.

To date, 95 Members of the WTO (counting the EU as one) have notified that they currently have CVD legislation in place, while 34 Members have not yet notified that they maintain such legislation. Among the notifications of CVD laws and regulations reviewed in 2002 were those of Antigua and Barbuda, Argentina, El Salvador, Georgia, Grenada, India,

Moldova, Myanmar, Pakistan, Peru, Philippines and Uruguay.[5] The notifications of the following Members were scheduled to be reviewed at the fall 2002 regular meeting but were postponed until next year: Antigua and Barbuda, Argentina, Brazil, Grenada, Japan, Lithuania, Taiwan, and Turkey.

As for CVD measures, eight WTO Members notified CVD actions taken during the latter half of 2001, and eight Members notified actions taken in the first half of 2002. The Committee reviewed actions taken by Argentina, Australia, Canada, the EU, Mexico, New Zealand, South Africa and the United States.

3. Extension of the Transition Period for the Phase Out of Export Subsidies

Under the Agreement, most developing countries were obligated to eliminate their export subsidies by December 31, 2002. Article 27.4 of the Agreement allows for an extension of this deadline provided consultations were entered into with the Subsidies Committee by December 31, 2001. The Committee has the authority to decide whether an extension is justified. In making this determination, the Committee must consider the "economic, financial and development needs" of the developing-country Member. If the Committee grants an extension, annual consultations with the Committee must be held to determine the necessity of maintaining the subsidies.[6] If the Committee does not affirmatively sanction a continuation, the export subsidies must be phased out within two years.

In an attempt to try and address the concerns of small exporter developing countries, a special procedure within the context of Article 27.4 of the Agreement, was adopted at the Fourth Ministerial Conference under which countries whose share of world exports was not more than 0.10 percent and whose Gross National Income was not greater than $20 billion could be granted a limited extension for particular types of export subsidy programs subject to rigorous transparency and standstill provisions. Members meeting all the qualifications for the agreed upon special procedures are eligible for a five-year extension of the transition period, in addition to the two years referred to under Article 27.4.[7]

---

[5] In keeping with WTO practice, the review of legislative provisions which pertain or apply to both AD and CVD actions by a Member generally took place in the AD Committee.

[6] Any extension granted by the Committee would only preclude a WTO dispute settlement case from being brought against the export subsidies at issue. A Member's ability to bring a CVD action under its national laws would not be affected.

[7] In addition to agreement on the specific length of the extension, it was also agreed at the Fourth Ministerial Conference, in essence, that the Committee should look favorably upon the extension requests of Members which do not meet all the specific eligibility criteria for the special small exporter procedures but which are similarly situated to those that do meet all the criteria. This provision was added at the request of Colombia.

Colombia, El Salvador, Panama and Thailand made requests for certain export subsidy programs under the normal extension process provided for in the Agreement. Antigua and Barbuda, Barbados, Belize, Bolivia, Costa Rica, Dominica, Dominican Republic, El Salvador, Grenada, Guatemala, Honduras, Jamaica, Jordan, Kenya, Mauritius, Panama, Papua New Guinea, St. Kitts and Nevis, St. Lucia, St. Vincent and Grenadines, Sri Lanka, and Suriname made requests for certain programs under the special procedures adopted at the Fourth Ministerial Conference for small exporter developing countries.[8] Uruguay requested an extension for one program under both the normal and special procedures. Additionally, Colombia sought an extension for two of its export subsidy programs under a procedure agreed to at the Fourth Ministerial Conference analogous to that provided for small exporter developing countries.

Altogether, the Committee conducted a detailed review of more than 70 export subsidy programs for which extensions were requested. Although nearly all of the requests were granted, some were eventually withdrawn and others were not approved for the full extension requested. (A chart showing how each of the requests were addressed is found in Attachment 2.) Throughout the review and approval process, the United States took a leadership role to define as narrowly as possible the scope of the extensions and to ensure that the conditions imposed on the extensions will strengthen the ability of the developing countries involved to come into compliance with their obligations upon expiration of the extension.

4. Other Implementation Issues

Two other implementation issues were addressed by the Committee in 2002: (a) a review of the Agreement's provisions regarding CVD investigations; and, (b) the methodology for the calculation of the per capita GNP threshold in Annex VII of the Agreement.

a. Review of the Provisions of the Agreement Regarding Countervailing Duty Investigations

The General Council first referred this topic to the Committee in August 2001. Brazil and India submitted papers making a large number of specific proposals concerning how to clarify or, in some instances, modify the provisions of the Agreement regarding CVD investigations. The proposals related to: the appropriate definitions of "domestic industry" and "like product"; the use of "facts available"; numerous calculation issues; and the conduct of annual reviews of CVD orders already in place. Due to the relatively short period of time

[8] Bolivia, Guatemala, Honduras, Kenya and Sri Lanka are all Annex VII countries and thus, may continue to provide export subsidies until their "graduation". Therefore, these countries have only reserved their rights under the special procedures in the event they graduate during the five-year extension period contemplated by the special procedures. Because these countries are only reserving their rights at this time, the Committee did not need to make any decisions as to whether their particular programs qualify under the special procedures.

prior to the Fourth Ministerial Conference, very little substantive discussion occurred with respect to the specific proposals made beyond the formal presentation of proposals. Thus, the Committee recommended to the General Council that the Committee continue to consider these issues and report to the General Council by July 31, 2002. This recommendation was adopted as part of the implementation decision adopted at the Fourth Ministerial Conference.

Pursuant to this mandate, the Committee held several meetings to address the procedural and substantive aspects of the review. The substance of the review was conducted on the basis of the proposals from Brazil and India tabled prior to the Fourth Ministerial Conference, as well as an exchange of written questions and answers. No consensus was reached concerning how to address these issues. Many Members, including the United States, suggested that the Rules Negotiating Group was the most appropriate forum to discuss these issues. The Committee Chair submitted his report to the General Council in July 2002, summarizing the Committee's discussions and noting that a consensus on resolution of the issues could not be reached.[9]

b. The Methodology for the Calculation of the Per Capita GNP Threshold in Annex VII of the Agreement

Annex VII of the Agreement identifies certain lesser developed countries that are eligible for particular special and differential treatment. Specifically, the export subsidies of these countries are not prohibited. Secondly, a higher *de minimis* threshold is provided for in CVD investigations of imports from these countries, although this standard expired at the end of 2002.[10] The countries identified in Annex VII include those WTO Members designated by the United Nations as "least-developed countries" (Annex VII(a)) as well as countries that had, at the time of the negotiation of the Agreement, a per capita GNP under $1,000 per annum and are specifically listed in Annex VII(b).[11] A country automatically "graduates" from Annex VII(b) status when its per capita GNP rises above the $1,000 threshold. When a country crosses this threshold, it becomes subject to the subsidy disciplines generally applicable to other developing countries.

Since the Agreement's entry into force in 1995, the *de facto* interpretation by the Committee of the $1,000 threshold was that it was expressed in current (*i.e.*, nominal or

---

[9] *See*, G/SCM/45, which can be obtained at http://docsonline.wto.org/gen_search.asp.

[10] The *de minimis* for Annex VII countries was 3 percent, compared with 2 percent for other developing countries.

[11] Annex VII(b) countries are Bolivia, Cameroon, Congo, Cote d'Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka, and Zimbabwe. In recognition of a technical error made in the final compilation of this list and pursuant to a General Council decision, Honduras' status as an Annex VII(b) country was formally clarified on January 20, 2001.

inflated) dollars. The concern with this interpretation, however, was that a country could graduate from Annex VII on the basis of inflation alone, rather than on the basis of real economic growth.

In 2001, the Chairman of the Committee, in conjunction with the WTO Secretariat, developed an approach based on certain World Bank data that were used by the Uruguay Round negotiators in 1990 in developing Annex VII(b). While many Members expressed the view that they could accept this proposed methodology, other Members indicated that it was more appropriate to rely on more recently available data. Thus, it was not possible to reach a consensus on the question of methodology.

At the Fourth Ministerial Conference, it was agreed:

> . . . that Annex VII(b) to the Agreement on Subsidies and Countervailing Measures includes the Members that are listed therein until their GNP per capita reaches US $1,000 in constant 1990 dollars for three consecutive years. This decision will enter into effect upon the adoption by the Committee on Subsidies and Countervailing Measures of an appropriate methodology for calculating constant 1990 dollars. If, however, the Committee on Subsidies and Countervailing Measures does not reach a consensus agreement on an appropriate methodology by 1 January 2003, the methodology proposed by the Chairman of the Committee set forth in G/SCM/38, Appendix 2 shall be applied. A Member shall not leave Annex VII(b) so long as its GNP per capita in current dollars has not reached US $1000 based upon the most recent data from the World Bank.[12]

In the course of 2002, no alternative methodology was proposed. Therefore, the Chairman's methodology proposed in 2001 will be applied in the future.

5. Areas of Focus in 2003

In 2003, the United States will continue to work with others to try to identify ways to rationalize the burdens of subsidy notification for all WTO Members without diminishing transparency or taking away from the other substantive benefits of the notification obligation. Second, the United States will participate actively in the review of other WTO Members' CVD legislation and actions, as well as China's Transitional Review Mechanism, and will bring to Members' and the Committee's attention any concerns which may arise about such laws or actions, whether in general or in the context of specific proceedings. The United States will also actively review any normal extension requests which may be made under Article 27.4 and will ensure the adherence to the provisions of the agreed upon extension procedures for small exporter developing countries. Finally, the United States is prepared to take a leadership role in addressing any technical questions that the Subsidies Committee

[12] The addition of the phrase "for three consecutive years" was added at the request of Honduras which was concerned that their possible graduation from Annex VII in the near future might place them in a worse condition than those Members which avail themselves of the special procedures under Article 27.4 for small developing-country exporters.

may be asked to consider in the context of issues that may arise within the Rules Negotiating Group.

B. CHINA: TRANSITIONAL REVIEW MECHANISM

The People's Republic of China became the 143rd Member of the WTO in December of 2001. In accordance with the terms of China's protocol of accession, the WTO created a special multilateral mechanism for a number of WTO councils and committees to review China's compliance with its WTO obligations on an annual basis. The first of nine WTO Subsidy Committee reviews due over a ten-year period under this Transitional Review Mechanism, or TRM, took place this past November. At this first review, the United States sought clarification from China regarding its compliance with WTO subsidy-related rules and disciplines. In this first critical year of China's accession to the WTO, we have also been closely monitoring and analyzing its subsidy programs and economic policies. As discussed below, China has made progress towards achieving WTO compliance with respect to its subsidy and pricing commitments, as well as its CVD legislation, but there remain areas deserving of improvement, particularly in terms of transparency.

1. Subsidy and Pricing Commitments

Upon its accession to the WTO, China agreed to eliminate all subsidy programs prohibited under Article 3 of the Subsidies Agreement; *i.e.,* export subsidies and import substitution subsidies. China also agreed to various special rules which apply when other WTO Members seek to enforce the disciplines of the Subsidies Agreement against Chinese subsidies.

At the time of its accession, China submitted a notification to the WTO of its subsidy programs, including those slated for elimination by virtue of its accession commitments. The Working Party report accompanying China's protocol of accession confirmed, however, that this notification was incomplete, and China committed to progressively work toward a full notification of subsidies. Nevertheless, China has not yet made any annual notification of its subsidies, as required under Article 25.1 of the Subsidies Agreement, the first of which was due last June 30 for the 2002 reporting period. During the transitional review discussions held at last fall's regular meeting of the WTO Subsidies Committee, the United States joined several other WTO members in urging China to submit its subsidy notification as soon as possible. China did, however, address and provide some responsive information in reply to a series of questions we posed concerning evidence and reports we had gathered about potential Chinese subsidy practices. In addition to calling for timely and informative compliance with WTO notification requirements, we have also provided technical assistance and training on CVD laws and WTO subsidy rules for various Chinese national and local government officials. We plan to continue these efforts throughout 2003, including the organization of a training program that would be held in China this Spring.

We are currently seeking more information regarding several existing or proposed Chinese programs and policies that, based on the general and secondary source information available to us, raise questions about their potential status as export subsidies or import substitution subsidies. The programs in question reportedly bestow (or would bestow) benefits to certain high technology products and the integrated circuit industry. When questioned about these programs during its transitional review, China stated it applies no specific policy to high-tech exports and that the integrated circuit industry program was not contingent upon export performance. We will continue to follow reports about these policies and practices, in addition to our general subsidy monitoring activities, focusing in particular on those sectors where Chinese government intervention may be of special concern for U.S. industries.

In addition to its commitments regarding subsidies, China also agreed that it would not use price controls to restrict the level of imports of goods or services and, in an annex to its accession protocol, listed the limited number of products and services remaining subject to price control or government guidance pricing. China agreed to attempt to reduce the number of products and services on this list, committing that it would not add additional products or services, except in extraordinary circumstances. The United States did not obtain the detailed information it requested from China on its use of price controls in 2002 during the transitional review. We will continue to seek such details and resolve any ambiguities through all appropriate and available mechanisms in 2003.

2. Countervailing Duty Legislation

China's accession agreement required it to revise its regulations and procedures for conducting CVD investigations and reviews to make them consistent with the rules set forth in the Subsidies Agreement. Shortly before China's accession, the State Council issued new CVD regulations which came into force on January 1, 2002. Later, China's Ministry of Foreign Trade and Economic Cooperation (MOFTEC), the government body with responsibility for determinations of subsidization under China's CVD regime, issued provisional procedural rules on initiation of investigations, questionnaires, verifications, and hearings. In December, the Supreme People's Court issued a judicial interpretation concerning the hearing and handling of CVD administrative cases, which took effect on January 1, 2003. The State Economic and Trade Commission (SETC), which determines injury in China's CVD investigations, subsequently issued procedural rules applicable to its proceedings. However, with the exception of the regulations themselves, none of China's procedural rules have been notified to the WTO, which hampers other Members' ability to confirm that such rules are consistent with China's WTO obligations.

While China's CVD regulations appear to be generally compliant with the WTO Subsidies Agreement, there are a few provisions which are ambiguously worded and warrant clarification. During the Subsidies Committee's transitional review of China's legislation, the United States and other WTO Members sought clarification of certain key issues including the definitions of "subsidy" and "specificity" under China's CVD regulations, the methods China will use to determine injury, and China's provisions for ensuring the

confidentiality of submissions while providing transparency. The United States will continue to seek needed clarifications of China's regulations and procedural rules through the Subsidies Committee and, as appropriate, through bilateral contacts. However, because China has never initiated a CVD investigation, either pre- or post-WTO accession, judgments about whether China's application of its CVD law and regulations would conform to WTO norms are premature.

C. WTO ACCESSIONS: U.S. MONITORING OF SUBSIDY-RELATED COMMITMENTS

Accession candidates to the WTO must provide detailed information concerning their economic and trade policies that have a bearing on WTO agreements. This information is reviewed by a Working Party of existing WTO Members dealing with a country's accession. Parallel negotiations are held between existing Members and the accession candidate to address bilateral trading interests. All interested WTO Members must be in agreement that their individual concerns have been met and that outstanding issues have been resolved in the course of their bilateral and multilateral negotiations before a new Member may accede.

The economic and trade information reviewed by the Working Party includes the accession candidate's subsidies regime. In the evaluation process, information on the candidate's use of subsidies and, in particular, the possible existence of prohibited subsidies is examined. In 2002, Commerce and USTR reviewed eighteen acceding countries' regimes for subsidy issues.[13] This information is found in a country's Memorandum on the Foreign Trade Regime, introduced at the beginning of the accession process. These facts are usually supplemented by outside research by Commerce and USTR to ensure complete information. Through a process of negotiation, issues are resolved and a mutually beneficial agreement is established.

The accession agreements recently finalized with Macedonia and Armenia offer two examples of how accession negotiations can help ensure the elimination of harmful, distortive subsidies. In both cases, a commitment was made by the acceding government to eliminate any prohibited subsidies and not to introduce such subsidies in the future. In the case of Macedonia, Commerce and USTR also obtained a commitment by Macedonia to provide an official interpretation of its legislation regarding Free Economic Zones, making clear that the use of domestic over imported goods was not a requirement to receive tax exceptions and incentives. Both Macedonia's and Armenia's agreements are awaiting ratification in their respective countries.

[13] The eighteen countries reviewed by the DOC and USTR in 2002 include: Algeria, Armenia, Azerbaijan, Bosnia, Cambodia, Cape Verde, Kazakhstan, Lebanon, Macedonia, Nepal, Russia, Samoa, Saudi Arabia, Ukraine, Uzbekistan, Vietnam, Yemen and Yugoslavia.

D. WTO TRADE POLICY REVIEWS

The WTO's Trade Policy Review Mechanism provides USTR and Commerce with another opportunity to review the subsidy practices of WTO Members. These reviews were agreed to as part of the Uruguay Round Agreements with the aim to (1) increase transparency and promote the understanding of other countries' trade policies and practices; (2) improve the quality of public and intergovernmental debate on important issues; and (3) enable a multilateral assessment of the effects of trade policy on the world trading system. These "peer reviews" encourage WTO Members to follow WTO rules and disciplines more closely and to fulfill their multilateral commitments. In general, Trade Policy Reviews (TPRs) focus on the particular country's trade policies and practices while also taking into account overall economic and developmental needs, policies and objectives, as well as the external economic environment that they face. The four largest traders in the WTO (the European Union, the United States, Japan and Canada) are examined approximately once every two years. The next largest 16 countries, based on their share of world trade, are reviewed every four years. The remaining countries are reviewed every six years, with the possibility of a longer interim period for the least-developed countries. For each review, two documents are prepared: a policy statement by the government under review, and a detailed report written independently by the WTO Secretariat. USTR and Commerce use TPRs to inquire about a wide range of issues, including Members' subsidy practices.

In 2002, USTR and Commerce reviewed fifteen Members' trade policy reports, including those of India, the European Union, Australia, Hong Kong and Japan.[14] With regard to subsidies, these reviews play an important role in ensuring that WTO Members meet transparency requirements concerning their subsidy practices, and the TPR provides a broader context than Subsidies Committee notification reviews in which to assess a Member's subsidy policies and their role in that Member's economy. In reviewing the trade policy reports, USTR and Commerce focus on the information concerning the subsidy practices detailed in the report, but also conduct extensive research on potential omissions regarding known subsidy practices that have not been reported. As noted above, this process is one additional measure by which the United States can effectively monitor worldwide subsidy practices and ensure that WTO Members comply with their obligations under the Subsidies Agreement.

E. MONITORING SUBSIDY PRACTICES WORLDWIDE

[14] The fifteen Members that were reviewed include: Guatemala, Pakistan, Malawi, Mexico, Slovenia, India, Barbados, the European Union, Mauritania, Australia, Dominican Republic, Zambia, Japan, Venezuela and Hong Kong. In 2003, sixteen Members will be reviewed. These include Maldives, El Salvador, Canada, Burundi, Southern African Customs Union, New Zealand, Morocco, Indonesia, Senegal/Niger, Honduras, Bulgaria, Guyana, Haiti, Thailand, Chile and Turkey.

One of the primary missions of the SEO is to monitor subsidy practices worldwide. Towards this end, we have continued to expand our comprehensive database of foreign government practices that are potentially actionable under the Subsidies Agreement. This information is made available to the public through the Internet on IA's home page. The Internet provides an easy and efficient avenue to reach U.S. businesses and other interested parties in order to furnish them with information previously available only in person in Washington. This allows U.S. producers and exporters to learn quickly about the remedies available to them under the Subsidies Agreement and to obtain the information necessary to develop a CVD case or a WTO subsidies complaint.

The SEO's electronic subsidies database provides information on all the foreign subsidy programs that have been investigated in U.S. CVD cases since 1980, covering more than 50 countries and over 2,000 government programs. The database is updated on a monthly basis, making information on subsidy programs investigated or reviewed by Commerce quickly available to the U.S. trading community. We will continue our efforts to ensure that information is promptly and accurately added to the database so it is easily available to the public. The site can be found at http://ia.ita.doc.gov/esel/eselframes.html. Attachment 3 shows the layout of the library and includes the list of countries about which information is available on the site.

The Subsidies Enforcement and IA sites also provide access to derestricted WTO subsidy notifications, listed by country, and easily accessible links to other useful U.S. and foreign government sites, such as USTR, the U.S. Export-Import Bank, the International Monetary Fund, the WTO (which maintains databases of Members' CVD actions, as well as their subsidy notifications to the WTO), the Canadian and Mexican government trade agencies, and the NAFTA secretariat. We are continuing our efforts to increase the number of useful U.S. government and foreign links provided.

Another advantage to integrating all of the subsidy information developed through years of conducting CVD investigations and subsidy information provided to the WTO is that USTR and SEO staff can easily check the WTO subsidy notifications of other countries and ensure that they are complete and accurate. As discussed in an earlier section of this report, the notification process is an important aspect of our subsidy enforcement efforts.

Finally, during 2002, SEO staff have been engaged in several focused areas of work concerning subsidy practices in various countries affecting specific industries in the United States. An overview of these efforts is provided in the "Advocacy and Enforcement" section of this report.

COUNSELING AND OUTREACH

A. ENFORCEMENT COUNSELING

USTR and Commerce SEO staff regularly respond to inquiries from, and meet with representatives of, U.S. industries concerned with the subsidization of foreign competitors. Our goal is to resolve problems arising from unfair foreign subsidization through a combination of formal and informal contacts with foreign governments. However, where appropriate, we will also advise U.S. companies of other remedies, such as a CVD investigation, WTO dispute settlement or an action taken under Section 301 of the Trade Act of 1974.

Enforcement counseling frequently starts with an inquiry by a U.S. exporter regarding a potential subsidy problem. As in prior years, we have continued to receive a number of these inquiries and, as a result, we are currently counseling and advocating on behalf of a number of U.S. exporters. The nature of the inquiries and information provided by U.S. companies to the agencies through these contacts varies greatly. In some cases, U.S. companies have simple questions concerning the Subsidies Agreement and U.S. rights under this Agreement. Other instances involve detailed complaints concerning specific subsidy practices and allegations that these practices have adversely affected U.S. companies' interests in either their U.S. or foreign markets. In these cases, our staff first discusses the subsidy problem with the exporter, and then gathers information about the practice and how the company's ability to sell in the United States or foreign markets may be affected.

The firm or industry in question is usually the best source of information concerning the harm resulting from the subsidization. This information is critical to support a claim of "serious prejudice," the more commonly used trade effects standard available in a WTO subsidy enforcement proceeding.[15] In most instances, we also conduct significant additional research to determine the legal framework under which the foreign government is offering the assistance and whether other U.S. exporters have been facing similar problems.

In order to develop as much information as possible about the subsidy practice, we draw on a wide range of internal and external sources (*see*, "Integration of Government Resources" section below). We start with general sources such as the SEO's Electronic Subsidies Library, the Internet and news organizations. Discussions with other Commerce

---

[15] As explained earlier, in order for subsidies, other than prohibited subsidies, to be actionable they must be specific (*e.g.*, provided to a single firm or industry or a group thereof) and cause adverse effects to the interests of another Member. Adverse trade effects can include (1) material injury to the domestic industry, or the threat thereof, as in CVD proceedings, (2) the nullification or impairment of benefits accruing directly or indirectly to another WTO Member under the GATT 1994, and (3) the displacement or impeding of sales or significant price undercutting, price suppression or price depression in so-called "serious prejudice" disputes brought to the WTO. Because serious prejudice can arise in any market affected by an actionable subsidy (whether in an importing country, the subsidizing country, or a third-country market), it is likely the standard that would most often be used to challenge subsidized competition in the subsidizing country or third-country markets.

offices that routinely collect information on specific country and industry practices, and Commerce's Advocacy Center[16] are also useful to learn whether any U.S. exporters have reported facing similar problems. If necessary, we will contact the U.S. embassy in the appropriate foreign country to discuss our findings and determine whether there is additional information that our posts abroad can provide. Sometimes it has also been useful to contact our counterparts in foreign governments to learn whether similar complaints about the same third-country subsidy practice have been identified by their exporters. Where appropriate, we may also seek public comment and/or consult with representatives of U.S. state and local governments.

Working with an interagency team, USTR and Commerce will then evaluate the information and determine the most effective way to proceed. As noted above, we have found that it is often advantageous to pursue resolution of these problems through a combination of informal and formal contacts. For example, raising the matter with the foreign government authorities through informal contacts, formal bilateral meetings and/or through discussions in the WTO Subsidies Committee may produce more expeditious and practical solutions to the problem than immediately resorting to WTO dispute settlement. These contacts may lead to additional information about the practice, which can affect the decision concerning the appropriate measures to take, including the possibility of pursuing the problem on grounds other than those provided for under WTO subsidy rules. However, if these efforts fail to bring a resolution to the issue, bringing a formal dispute settlement action in the WTO remains a viable option for some cases.

B. INTEGRATION OF GOVERNMENT RESOURCES

Throughout 2002, the SEO continued to ensure that government personnel who have daily contact with the U.S. exporting community, both in the United States and abroad, are aware of the resources and services available regarding subsidy enforcement efforts. An important aspect of these efforts involves the deepening interaction and coordination between SEO and TRCS staff. Together, SEO and TRCS staff work to identify, track and, where appropriate, address various foreign government policies, business practices and trade trends that may contribute to the development of subsidy and other unfair trade problems.

1. Trade Remedy Compliance Staff

As foreshadowed in last year's report, the government-wide trade compliance and market access initiative that was begun in 2001 has just completed its first full year of

[16] The Advocacy Center helps U.S. exporters seek contracts abroad on an equal footing with foreign government-backed competitors.

operation, resulting in, among other things, the placement of various new personnel in posts abroad to enhance the effectiveness of U.S. monitoring and enforcement of trade agreements, including the Subsidies Agreement. The establishment of the TRCS, as discussed in last year's report, fulfills that aspect of the trade compliance initiative which is focused on enforcement of multilateral subsidy rules and addressing unfair trading practices. TRCS is now fully engaged in supporting and complementing the work of the SEO. Attachment 4 contains a full description of the TRCS and its duties.

In keeping with Congressional directives, senior IA officers are now in place in Beijing and Seoul, with plans to station additional personnel in Japan being finalized. These overseas officers work closely with their colleagues in the embassies and with TRCS personnel headquartered in Washington to identify and evaluate potential unfair trade problems. Through such proactive efforts, Commerce can facilitate the application of U.S. unfair trade remedies, help to pinpoint and modify foreign practices and policies that lead to unfair trade, and neutralize disputes that could otherwise heighten trade frictions. Although the TRCS devotes much of its focus to tracking developments concerning the United States' main trading partners in Asia (*see,* section above concerning monitoring of China's WTO obligations), its contributions to the international efforts to address steel market distorting practices and in monitoring foreign trade law enforcement affecting U.S. exporters have led to an increasingly global focus.

As determined by IA headquarters, overseas IA officers may carry out a variety of responsibilities related directly to the administration of the U.S. AD/CVD laws. For example, they may present questionnaires to foreign firms and governments in AD/CVD investigations and administrative reviews; verify or facilitate the verification of responses to such questionnaires; provide technical support for the negotiation and monitoring of suspension agreements of AD/CVD proceedings; assist in the identification, analysis and handling of circumvention allegations concerning AD/CVD measures; and serve as an in-country source of guidance and information for host-country firms participating in such investigations and reviews.

However, beyond these duties, both the overseas officers and the Washington-based TRCS staff help to explain the U.S. system of unfair trade law enforcement to the foreign audience, whether that be government officials, business representatives, or other interested groups. For example, the TRCS recently hosted meetings on AD/CVD methodology for officials of the Korea Trade Commission, and our officers in Beijing have briefed a variety of government and private sector audiences on U.S. AD/CVD laws and practices. These types of interactions help to promote a better understanding of U.S. unfair trade laws and policies, as well assist foreign firms and governments in avoiding unfair trade problems with the United States. Also, they contribute to fuller and more effective participation in U.S. investigations and administrative reviews – a development which should mutually benefit the foreign parties and U.S. investigators, and generally improve the quality of investigative results.

As noted above, the expertise of TRCS personnel has also been employed to more closely monitor foreign governments' use of unfair trade remedies, especially in situations affecting U.S. exporters, and to offer technical assistance to foreign AD/CVD authorities in an effort to enhance their transparency and respect for due process in applying WTO-sanctioned trade remedies. In the fall of 2002, TRCS developed, coordinated and conducted an extensive technical assistance program in Washington for a group of scholars from the Shanghai WTO Affairs Consultation Center. We plan to hold similar training for future classes of Shanghai Center scholars visiting Washington in the coming years, and are using the training modules as a starting point for fashioning a technical assistance program in consultation with China's own AD/CVD law administrators in MOFTEC and SETC.

2. Subsidies Enforcement Outreach Efforts Overseas

The SEO conducts frequent outreach programs to ensure that government personnel who have daily contact with the U.S. exporting community, both in the United States and abroad, are aware of the resources and services available regarding subsidy enforcement efforts. Within Commerce, the U.S. Commercial Service (USCS) is charged with counseling U.S. companies through its network of domestic and foreign posts. SEO staff hold formal briefings with USCS officers on rotation in Washington to explain the types of services and information offered by the SEO. We also provide USCS officers with handouts detailing SEO activities and contact information. These are used by the officers at their overseas posts to inform other USCS officers and visitors from the U.S. business community about our resources (*See,* Attachment 5.) SEO staff also benefit from information provided by USCS officers during these briefings about the types of subsidy problems U.S. companies are facing in the host countries. In addition, SEO personnel participate in special conferences for senior commercial officers and training sessions held for foreign service national employees[17] in Washington. These meetings allow SEO staff to inform a large number of government officials who have daily interaction with U.S. companies about the resources the SEO can offer.

The SEO also works closely with the U.S. Department of State and U.S. Department of Agriculture to involve foreign service economic and agriculture officers in subsidies enforcement activities. This fulfills our statutory mandate to secure the cooperation of other federal agencies in these activities, as provided for in section 281(g) of the URAA. To this end, USTR and SEO personnel train foreign service officers on how to identify and evaluate foreign subsidy practices that may be inconsistent with the Subsidies Agreement and that may involve unfair trade actions against U.S. companies. Cooperation of this type occurs not only in specific cases initiated by the SEO or USTR, but on an ongoing basis whereby foreign service officers develop and share information with Commerce, USTR and the interagency team concerning foreign government subsidy practices and the administration

[17] Foreign service nationals are professional employees of U.S. embassies and consulates who are natives of the country in which the embassies are located. These employees assist foreign service and USCS officers with their assigned duties.

of foreign governments' unfair trade laws.[18] This type of collaboration between Departments is critically important to help effectively enforce the Subsidies Agreement.

Embassy-based personnel offer a unique perspective to our subsidy enforcement efforts. USCS officers have daily contact with the U.S. exporting community and, therefore, are directly aware of the problems facing the companies. Foreign service officers often have key insights about the types of subsidy programs being administered, implemented or contemplated by the host governments. The type of information provided by U.S. embassy staff has proven to be very useful in determining the most appropriate areas in which to focus our efforts to assist U.S. exporters. These efforts have obviously been enhanced by the addition of TRCS officers to certain posts, where they have been welcomed by their foreign service and USCS colleagues and can contribute their technical expertise about AD/CVD and subsidies issues to the embassy's overall analysis of and recommendations concerning a particular issue. We look forward to expanding these synergies further in the years ahead.

3. Other Coordination Efforts

SEO staff also maintain close contacts within Commerce's International Trade Administration (ITA), in particular the country and industry desk officers, the Advocacy and Trade Compliance Centers (TCC), and the Compliance Coordinators Group (CCG). The CCG is comprised of representatives from all of ITA's units (Market Access and Compliance, Trade Development, IA, and USCS) and the Patent and Trademark Office, and serves as the central coordinating point for ITA's market access and agreement compliance activities. The group meets regularly to share information on trade compliance and market access issues that may be common across regions or industrial sectors, and works to resolve these issues by drawing upon the full range of expertise available within ITA. Such contacts allow us to ensure that these offices are fully appraised of the SEO's subsidy enforcement activities and that they provide SEO staff with information that they routinely collect.

An example of the collaborative effort within ITA on subsidies enforcement is the SEO's work with the TCC and the Advocacy Center. The TCC monitors compliance with active international agreements covering manufactured goods and services to which the United States is a signatory. Complaints received by the TCC that may involve foreign subsidies are immediately referred to the SEO for analysis and action. The Advocacy Center assists U.S. exporters seeking government contracts abroad by providing U.S. government advocacy on behalf of the U.S. company when foreign competitors bidding on the same contract enjoy support from their governments. At times, this foreign government

[18] As described above, an important factor in a U.S. company's ability to do business in any given market is the manner in which the foreign government administers its unfair trade laws and, in particular, its CVD and AD laws. IA monitors these foreign AD and CVD actions involving U.S. companies to ensure that the foreign governments are conducting these investigations in accordance with their international obligations.

support may be in the form of subsidies. When the Advocacy Center receives a call from a U.S. company concerning possible foreign government subsidization, the Center contacts the SEO and provides all of the relevant information. In addition, the Advocacy Center has connected the SEO to its computer database. This allows us to review information gathered by the Center to determine whether U.S. exporters' access to foreign contracts is being impeded by government practices which may be actionable under subsidy rules.

C. OTHER TECHNICAL ASSISTANCE

A number of the sections above outline USTR and Commerce's extensive technical assistance efforts, for example with regard to training Chinese national and local government officials, and in the context of WTO accession negotiations. During 2002, USTR and Commerce were engaged in additional technical assistance efforts with developing countries and countries that have completed the transition to market economy status.

1. Subsidies Training for Newly Designated Market Economies

In 2002, Commerce reached decisions to treat the Russian Federation and Kazakhstan as market economies for the purpose of AD duty investigations. Prior to those decisions, these countries were subject to special AD duty methodologies reserved for non-market economies. As a result of this new designation as market economies, the Russian Federation and Kazakhstan also became subject to potential action under the U.S. CVD law. Because of their unfamiliarity with the WTO Subsidies Agreement and the U.S. CVD statute, these countries invited Commerce officials to provide training programs focusing on WTO rules and obligations concerning subsidies and CVD investigations. Calculation methodologies and procedures for identifying and evaluating foreign subsidy practices were also extensively reviewed. These training programs help to strengthen our ties with foreign officials, and ensure that the administration of trade remedy laws by our trading partners is consistent with their international obligations.

2. Subsidy Notifications

As noted above, Members agreed to a three-prong strategy to address the ongoing difficulties experienced by Members in meeting the subsidy notification obligations under Article 25 of the Subsidies Agreement. The third prong was the organization of a subsidy notification seminar with the purpose of bringing together capital-based officials from all Member countries that were responsible for subsidy matters and for subsidy notifications. With a view toward ensuring maximum participation, including those developing country Members with resource constraints, the WTO's technical assistance fund provided financial support for one capital-based official from 36 lessor-developed country Members and Observers, as well as a number of additional capital-based officials from developing country Members. The aim of the seminar was to have a detailed discussion of the notification obligations and to exchange experiences and ideas in order to improve understanding of the

notification obligations and identify ways in which Members could streamline and facilitate the preparation of notifications. U.S. officials participated as panelists in the October 2002 seminar. We shared with officials from developing countries strategies used to prepare the U.S. notification, with emphasis on practical solutions to the knowledge and resource constraints faced by many Members. This seminar provided an excellent opportunity for capacity building and technical assistance, with the potential benefit of enhancing transparency among WTO Members' subsidy practices.

ADVOCACY AND ENFORCEMENT

A. ADDRESSING FOREIGN SUBSIDIES AFFECTING U.S. INTERESTS

The United States pursues enforcement of U.S. rights under the Subsidies Agreement through WTO dispute settlement proceedings, bilateral contacts and other actions. Although any decision to initiate a dispute settlement proceeding must carefully take account of the balance of U.S. interests, our general and overarching policy objectives remain aimed at discouraging distortive subsidization and preventing or remedying harm caused to U.S. producers and workers by such subsidies. These objectives are expressed clearly in the URAA, and they provide the context in which potential subsidy enforcement complaints have been, and will continue to be, considered. USTR and Commerce work closely with one another and with the full range of federal agencies – such as the Departments of State, Treasury and Agriculture – in fulfilling this mission. This interagency cooperation is also crucial to the success of our efforts to protect and defend U.S. interests in other circumstances involving subsidy rules, such as in the explanation and defense of U.S. measures targeted by others in WTO dispute settlement and in the assistance we provide to U.S. exporters and respondent agencies subject to foreign CVD actions. In the following section, we summarize some of the principal subsidy-related disputes and activities in which the United States has been involved over the past year.[19]

1. Hynix Semiconductor, Inc. of Korea

In the Subsidies Enforcement reports of 2001 and 2002, we detailed our ongoing efforts to monitor and proactively address what has appeared to be recurring Korean government aid to its semiconductor industry, specifically Hynix Semiconductor, Inc. (Hynix). Over the course of the past year, Hynix was the beneficiary of additional debt-for-equity swaps and debt forgiveness through additional restructuring engineered by its main creditors, including several in which the Korean government maintains ownership or significant control. In July 2002, the European Commission, at the request of Infineon Technology AG of Germany, initiated a CVD investigation of Dynamic Random Access Memory (DRAM) chips imported from Korea in which the chief respondents are Hynix and

[19] Information about WTO dispute settlement proceedings is available to the public on the World Wide Web at: http://www.wto.org/wto/english/tratop_e/dispu_e/distab_e.htm.

Samsung Electronics. In November, Commerce initiated a CVD proceeding on DRAMs imported from Korea in order to investigate alleged subsidies received by Hynix as well as Samsung.[20]

In late December, Hynix's creditors, following suggestions made by its advisor Deutsche Bank, organized an additional debt relief package potentially including a $1.58 billion debt-for-equity swap and a roll-over of Hynix's $2.5 billion of debt by 2006. Furthermore, Hynix creditors agreed to provide financing for a Chinese firm to take over a Hynix subsidiary, thereby indirectly facilitating a direct cash infusion to Hynix. In view of the magnitude of the package and the history of intervention with respect to Hynix, the U.S. government has expressed renewed concern both about this rescue package, led by government-owned and -controlled Korea Development Bank, and about the reliability of the Korean government's commitment to market reform and permitting market forces to determine the fate of heavily-indebted Hynix. We will continue to closely monitor the Hynix situation.

2. Textiles Initiative

a. General

In January 2002, Secretary Evans announced the formation of an interagency textile working group (TWG), chaired by Commerce Under Secretary for International Trade Grant Aldonas. The TWG established seven subgroups to address the commitments made by Secretary Evans to the House textile caucus in December 2001. SEO staff have actively participated in the subgroup dedicated to strong enforcement of U.S. trade remedy laws generally, and on behalf of our textile industry in particular. Our efforts to date have been multi-faceted. First, as mentioned in other sections of this report, we have a strong, affirmative agenda in the WTO rules negotiations aimed at preserving the effectiveness of trade remedy rules, deepening and expanding disciplines on trade-distorting practices, and ensuring the same high standards of transparency and due process in foreign trade regimes as those that are respected under U.S. law. Second, SEO staff have met separately with U.S. textile industry representatives to explain AD and CVD procedures and analyze options available to the industry under U.S. trade remedy laws. We also provided an in-depth briefing to the Industry Sector Advisory Committee for Textiles and Apparel on these issues. Third, we have conducted research into potentially countervailable/actionable subsidies provided to textile manufacturers and exporters in certain textile exporting countries. We are continuing to explore several possible WTO strategies to address the problem of such potentially distortive subsidies to foreign textile exporters.

b. "Export Competitiveness" Calculation Request on Indian Textiles

[20] The preliminary determination in the U.S. CVD investigation is scheduled for March 31, 2003.

As part of our ongoing efforts to utilize fully the Subsidies Agreement to address the U.S. textile industry's concerns regarding unfair subsidy practices, SEO and USTR staff developed a U.S. request that was submitted to the WTO Secretariat in late January 2003, regarding India's textile manufacturing exports. As noted earlier, the Subsidies Agreement provides for special and differential treatment of developing countries specifically listed in Annex VII of the Agreement, which allows these countries to maintain export subsidies until their GNP per capita reaches a specified amount. However, under Article 27.6 of the Agreement, once a product of an Annex VII country, such as India, reaches "export competitiveness," any export subsidies given on that product must be phased out over an eight-year period. Article 27.6 defines export competitiveness as the point when an exported product reaches a share of 3.25 percent of world trade for two consecutive calendar years.

Using United Nations trade data, SEO staff, working with the Commerce's Office of Textiles and Apparel, identified specific textile and apparel product categories that we believe are above the export competitiveness threshold for India. We have also identified several export subsidy programs which we believe are benefitting India's textile and apparel manufacturers. The WTO Secretariat, in its May 2002 Trade Policy Review of India,[21] identified Government of India assistance programs available to textile exporters. Several of these programs have been investigated by the Commerce in CVD investigations involving non-textile-related Indian exports, and have been found to constitute export subsidies.

Our submission to the WTO requests that, pursuant to Article 27.6, the Secretariat perform a computation of India's export competitiveness for its textile exports. While the computation of export competitiveness is a purely technical exercise that does not involve dispute settlement, an affirmative finding will require India to phase out any export subsidies on such products over an eight-year period.

SEO and USTR staff intend to continue examining whether other countries provide subsidies on their textile exports and will make full use of the disciplines of the Subsidies Agreement to address our industry's legitimate concerns.

3. Subsidies Provided to the Fertilizer Industry

USTR and the SEO have continued their close cooperation with U.S. exporters of diammonium phosphate (DAP), a fertilizer product, to address Indian fertilizer subsidies. These subsidies provide benefits to Indian producers of DAP that the U.S. industry believes adversely affect its ability to export to the Indian market. Under the subsidy program, domestic producers and foreign suppliers are paid the difference between the controlled retail price and a government-established amount. However, the Indian subsidy program provides a higher level of subsidy payment to domestic producers than to importers of DAP.

---

[21] *See*, "Trade Policy Review - India, Report by the Secretariat", WT/TPR/S/100, May 22, 2002, pg. 112.

The U.S. industry is also concerned with India's failure to publish timely information about the subsidy amounts. The non-transparent and retrospective nature of the program's administration further undermines the U.S. industry's ability to export effectively.

In October 2001, SEO and USTR personnel first approached Government of India ("GOI") officials to express serious concerns regarding the Indian subsidy program. As our informal discussions did not lead to a satisfactory resolution, in April 2002, we submitted formal questions via the WTO Subsidies Committee on India's fertilizer subsidy scheme. The GOI provided a partial response to our queries on November 1, 2002. We are reviewing that response to determine whether additional questions are necessary. Throughout 2002, SEO staff also have worked closely with other Commerce offices to ensure that the DAP subsidy issue was raised at every appropriate meeting with responsible Indian government officials.

To date, our aim has been to obtain a practical resolution that avoids WTO dispute settlement. Recent statistics indicate, however, that U.S. exports have declined substantially. Over the past decade, the United States had supplied approximately 70 percent of India's DAP imports. As the subsidy differential has increased, the volume of U.S. DAP exports to India has plummeted from 2.2 million metric tons in 1999 to just 200,000 metric tons through October 2002. The U.S. industry has noted that India's fertilizer policy is a significant market access impediment and that a timely resolution of this issue is necessary. We will continue to work with the U.S. industry and examine closely the DAP subsidy program and the adverse effects it appears to be causing, as well as all possible avenues available to address this problem.

4. Canada: Export Subsidies and Tariff-Rate Quotas on Dairy Products

In early 1998, the United States, later joined by New Zealand, commenced a WTO dispute settlement proceeding involving subsidized exports of dairy products by Canada. That proceeding culminated in the October 1999 adoption by the WTO's Dispute Settlement Body of the recommendations made in the Appellate Body and panel reports. Those reports found that Canada's two-tier pricing system for milk constituted an export subsidy under the provisions of the Agreement on Agriculture and that Canada had during 1997 and 1998 exported more subsidized dairy products than was permitted by its commitments under the Agriculture Agreement. The legal reasoning in those reports confirmed that governments cannot avoid their export subsidy commitments under the Agreement on Agriculture by entrusting authority to quasi-government entities. Along the lines of the definition of a subsidy described in Article 1.1(a)(1)(iv) of the Subsidies Agreement, the panel concluded that when governments delegate powers to such entities and such bodies perform governmental functions, their actions are no less governmental than had the government undertaken the acts.

In December 1999, the United States, Canada and New Zealand concluded an agreement establishing the time frame within which Canada would implement the DSB recommendations and bring its export subsidy programs into compliance with its obligations

under the Agreement on Agriculture. Pursuant to that agreement, Canada changed several parts of its dairy program, including the elimination of one category of export subsidies – those which provided for the subsidized export of products made from surplus milk. However, individual Canadian provinces, working with the federal government, introduced substitute programs under which exporters obtained milk at prices that are below domestic market levels in Canada.

In February 2001, the United States and New Zealand requested review of the new Canadian programs pursuant to Article 21.5 of the Dispute Settlement Understanding. At the same time, the United States and New Zealand requested authorization to withdraw concessions pursuant to Article 22 of the Dispute Settlement Understanding. Consideration of that request, however, was suspended pending completion of the Article 21.5 compliance review.

In July 2001, the Article 21.5 panel released its report in which it found that the continued involvement of Canadian federal and provincial governments in the provision of low-cost milk to processors for export constituted an export subsidy and that Canada had already exceeded its commitment under the WTO Agriculture Agreement on subsidized cheese exports. Canada appealed the panel report. In October 2001, the WTO Appellate Body issued its report in which it disagreed with the panel on certain legal points but found that it was unable to reach a decision on the legality of the dairy export program due to an incomplete factual record.

In response, the United States and New Zealand filed a second request pursuant to Article 21.5 for another panel review in order to present additional factual information. On July 26, 2002, the second Article 21.5 panel found that the steps Canada took to implement the adverse findings regarding its dairy export practices were insufficient and that Canada continued to provide export subsidies on dairy products at a level that exceeded its export subsidy commitment levels under the Agreement on Agriculture. Canada appealed the panel's findings. On December 20, 2002, the Appellate Body upheld the panel's findings. The DSB adopted the Appellate Body and panel reports in January 2003.

5. European Union Support for Development of the Airbus A380 Aircraft

In 2002, the United States and the European Union held consultations concerning the provision of EU government financial assistance for the Airbus A380 jetliner project and other issues regarding trade in large civil aircraft. The European Union furnished additional information to supplement its initial notification of government financial assistance for the Airbus A380 program, which was provided under the 1992 U.S.-EU Agreement Concerning the Application of the WTO Agreement on Trade in Civil Aircraft to Large Civil Aircraft. Further information continues to be sought on how this government support comports with the obligations of this agreement and the Subsidies Agreement.

6. Canadian Wheat

On February 15, 2002, responding to a complaint filed by the North Dakota Wheat Commission (NDWC), USTR announced a four-prong approach to fight for a level playing field for American farmers. First, on December 17, USTR announced that the United States was filing a case against Canada in the WTO over the wheat trading practices of the monopolistic Canadian Wheat Board (CWB). In addition, the United States is challenging as unfair and burdensome Canada's requirements to segregate imported grain in the Canadian grain handling system, along with Canada's discriminatory policy affecting U.S. grain access to Canada's rail transportation system.

Second, the Administration committed to review antidumping and countervailing duty petitions filed by the North Dakota Wheat Commission on September 13, 2002. The Administration initiated investigations on those petitions on October 23, and the U.S. International Trade Commission determined that there is a reasonable indication that U.S. industries are materially injured or threatened with material injury by imports of durum wheat and hard red spring wheat from Canada on November 19, 2002.

Third, USTR indicated it would work to identify impediments to U.S. wheat entering Canada. The U.S. request for consultations on Canada's segregation and rail transportation systems for grain is a result of that investigation. Fourth, the U.S. committed to seek reform in global trade negotiations in the WTO agriculture negotiations. The United States has aggressively pursued permanent reform of monopolistic export state trading enterprises, such as the CWB, in the WTO agriculture negotiations that are part of the Doha Development Agenda.

7. Subsidies Provided to the Fisheries Industry

Fisheries experts and intergovernmental organizations have increasingly begun to recognize the important role that subsidies play in contributing to the problems of overcapacity in the fisheries industry which, in turn, have been a major contributor to an alarming depletion of the world's fish stocks. These subsidies, and the depletion of fisheries resources, are also adversely affecting international fish trade. In response, the harmful effects of fisheries subsidies have been taken up as an area of focus on a number of different policy fronts and in a variety of international fora. In addition to the discussions in the WTO Rules Negotiating Group, the WTO Committee on Trade and Environment (CTE) along with the UN Food and Agriculture Organization (FAO) continue to examine the role government subsidies play in the fisheries sector. Likewise, other intergovernmental organizations, including the World Bank, the OECD and the Asia Pacific Economic Cooperation (APEC) forum have been conducting work on estimating the levels, and to some extent the effects, of subsidies worldwide. The importance of this work on fisheries subsidies was also underscored at the August 2002 World Summit on Sustainable Development in South Africa, where world leaders called for action on a number of fronts, including the elimination of harmful subsides, to maintain or restore world fish stocks to sustainable levels.

Throughout 2002, Commerce and USTR worked with other federal agencies to gather and analyze information and to express views and concerns across the range of international organizations focused on fisheries subsidies. For example, as noted earlier in this report, we are pursuing a strong agenda in the WTO Rules Negotiating Group to institute more effective international rules on fisheries subsidies in the context of the Subsidies Agreement. We are also closely following and participating in the ongoing work at the CTE, OECD, FAO, and APEC on fisheries subsidies, with an eye towards identifying and pursuing areas in which the work in each of these organizations can be mutually reinforcing. Furthermore, in addition to compiling and submitting our own notification of fisheries subsidies in the most recent U.S. notification of subsidies under Article 25 of the Subsidies Agreement, Commerce and USTR spent a significant amount of time in the past year reviewing and analyzing the fisheries subsidies notifications of Member countries. Though complete and timely notification of all subsidies is an important responsibility of all Members, this is particularly true in the case of reporting fisheries subsidies, because these notifications are one of the sources of information on which experts rely in determining the scope and appropriate response to these problems.

Commerce and USTR also remain actively engaged in addressing the impact of foreign fisheries subsidies on U.S. economic and environmental interests. In the past year, for example, a group of industry representatives expressed concern over the deleterious effect of certain foreign fishing practices, encouraged in part by foreign subsidies, on U.S. commercial and recreational activities involving Atlantic bluefin tuna, Atlantic white marlin, and Atlantic swordfish. We continue to raise our views on these and related concerns with other countries at the highest levels, and are prepared to examine the full range of possible actions to protect U.S. interests. We are committed to finding resolution to these problems and, as appropriate, will continue to actively pursue action on a range of fronts.

8. Government Support to Paper Production in Korea

SEO and TRCS staff have expanded their work since last year with the American Forest & Paper Association (AF&PA) to explore and address U.S. paper industry concerns about the adverse effects of targeted government aid to Korea's coated paper sector. A significant percentage of Korean coated paper output is exported to the United States and other markets. In light of this pronounced export orientation, U.S. coated paper producers are concerned that recurring instances of what appears to be inappropriate Korean government support and intervention for nonviable enterprises may be distorting international markets for paper goods. Among the examples of intervention that have been cited and that are now under scrutiny are: low-cost facility investment loans and loan guarantees; tax benefits for facility expansion; government sponsored creation of a paper manufacturing complex; and government sale of debt obligations.

SEO and TRCS staff are evaluating evidence made available by the U.S. industry and its counsel, as well as information gathered internally, to clarify the situation and determine the extent and impact of possible subsidization. In November, AF&PA organized a visit to a U.S. coated paper mill for SEO and TRCS officials so that they could better

understand the product and the processes involved in coated paper production, and could hear first-hand about the impact of Korean trade on the U.S. industry.

Based on the data collected and analyses made thus far, U.S. government concerns have been communicated bilaterally to Korean government officials at both the working and political levels, including at quarterly trade meetings, and raised in the regular fall meeting of the WTO Subsidies Committee. In addition, we posed a series of questions to Korean authorities that were designed to permit a fair and full assessment of the nature of Korean government involvement and whether any WTO obligations have been violated. Korean authorities have thus far denied any WTO-inconsistent actions, but have provided only general replies to the questions we submitted. We are studying those replies carefully, in conjunction with other information at our disposal, and plan to consult closely with the U.S. paper industry as we consider options for possible further action.

9. Poland's Steel Restructuring Plan

The Polish government has embarked on a major restructuring and consolidation of its steel industry, which has been struggling to compete on the European and international markets and which amassed large amounts of debts after continued weak profitability. The restructuring plan has been carried out under the review and approval of the European Commission in the context of the broader process of Poland's accession to the European Union.

It appears that a major goal of this restructuring is to put the steel company Polskie Huty Stali (PHS) on a stronger financial and commercial footing so that the company can finance modernization and new investment and, thereby, be more attractive to potential bidders in a future privatization. The overall plan ultimately envisions some reduction in overall steel capacity, production specialization by mill, modernization of certain facilities, and cuts in employment. The government is taking several steps to achieve these goals. One important early step was the merging in 2002 of four of the leading state-owned steel companies, together accounting for about 70 percent of Poland's steel production, to form the single new company PHS. Another key step in the process is the reduction of existing corporate indebtedness. Prior to consolidation, the four companies that comprised PHS had a combined debt exceeding $1.26 billion. A variety of measures are planned in order to "clean up" the finances of PHS and other Polish steel companies, including massive debt forgiveness, debt-to-equity conversions, and the granting of preferential loans and loan guarantees. With regard to capacity, the plan calls for a roughly 900,000 ton cut in Poland's overall steelmaking capacity. However, capacity in certain product categories will in fact be increased. This entire restructuring process will be facilitated in large part through government subsidies on the order of $800 million, to be provided through 2006.

Given the planned size of the government subsidies involved, and the impact this could have on U.S. steel interests, Commerce and USTR are monitoring this restructuring process closely and have raised our questions about this plan in discussions with Poland's government and the European Commission. We recognize that restructuring of the Polish

steel industry is an important part of the overall health of Poland's economy and is a necessary step in the process of Poland's accession to the European Union. We have stressed, however, that Poland and the European Union must proceed in a way that is consistent with Poland's international obligations, including its obligations under the Subsidies Agreement. We will request from Poland and the European Commission additional up-to-date details as this process unfolds.

10. Update - Government Aid Programs Potentially Benefitting the Cattle and Beef Industries in Selected Countries

a. Introduction

In 2002, the SEO continued its efforts to identify and monitor potential subsidy practices in several major cattle and beef trading countries. Such practices may unfairly enhance exports from those countries to the U.S. market or work to impede market access abroad for U.S. cattle and beef exports. The importance of gathering and disseminating this information is highlighted by the essential role of cattle and beef in the agricultural sector, as well as the importance of agriculture issues in ongoing trade negotiations. SEO staff conducted the initial study of possible subsidy programs available to cattle and beef producers following a request made by 19 Senators in 2000. That report, appended to the 2001 SEO Annual Report to the Congress, examined potential subsidies and other aid programs provided to foreign cattle and beef producers in the following countries: Argentina, Australia, Brazil, China, the EU, Japan, Korea, New Zealand, and Uruguay. Last year's report updated the original research and noted changes in several countries' practices.

In 2002, SEO staff worked with representatives of the U.S. cattle industry to better understand the effect of trade policies on the domestic market. In January, SEO staff spoke at the Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA) Annual Convention in Billings, Montana. The discussion provided information on subsidy programs and their potential effect on U.S. imports and exports of live cattle and beef. In September, SEO staff traveled to South Dakota and Nebraska to meet with ranchers and feedlot operators to discuss the impact of trade on the industry and gather first-hand information on both the live cattle industry and the challenges facing independent ranchers today. In March and December, SEO and IA staff met with R-CALF USA representatives in Washington to discuss issues related to ongoing trade negotiations.

Information on the programs maintained by cattle- and beef-producing nations was obtained from a wide range of sources, including official government documents, WTO and OECD reports and, where available, foreign government statistics and other primary sources. Commerce officials also consulted directly with overseas U.S. embassy officials and cattle and beef experts from USDA's Foreign Agricultural Service (FAS). Additional information was provided by representatives of the U.S. cattle industry. This year's report includes descriptions of new programs and updates on those programs that underwent administrative or budgetary changes in 2002. It should be noted that mention of a

government aid program in this update in no way prejudges the status of that measure under WTO rules and/or whether it is actionable under those rules or U.S. law.

b. Background

Animal health issues continued to influence world trade in cattle and beef in 2002. While cattle and beef remained safe and trade patterns remained generally stable within North America, production and consumption were affected by lingering problems related to both bovine spongiform encephalopathy (BSE) and foot and mouth disease (FMD) in parts of Europe, Latin America, and Asia. This, in turn, influenced subsidy policies in several major cattle-producing countries.

In the United States, imports of beef slowed substantially in late 2002 after posting three percent growth in the first half of 2002. Several conditions, including drought and somewhat lower demand for hamburger beef, contributed to the reduction in import growth. Overall, imports in 2002 are expected to approximate those of 2001. The Department of Agriculture predicts 2003 imports will exceed 3.3 billion pounds, due primarily to growth in demand and a reduced slaughter of domestic cattle stock.[22] Imports of beef from Canada are forecast to increase, and both Australia and New Zealand are expected to fill their Tariff Rate Quotas (TRQs) in 2003.

U.S. exports of beef are forecast to increase slightly, to 1.15 million metric tons, in 2003. Reduced beef supply resulting from the predicted smallest U.S. cattle herd in decades will be the primary limiting factor in increasing export growth further.[23] Through October 2002, live cattle imports from Mexico were down by approximately 40 percent in value terms, while imports from Canada increased. The value of U.S. live cattle exports to both countries decreased during the same period. [24]

The TRQ system for imports of fresh, chilled and frozen beef into the United States was unchanged in 2002. Under the TRQ, 696,420 metric tons of beef can enter the U.S. market at zero duty. A 26.4 percent tariff goes into effect when countries fill their allocated share of the TRQ. Australia is allocated the majority (378,210 metric tons) of the total beef TRQ, followed by New Zealand with approximately 30 percent (213,400 metric tons). The remaining TRQs are divided among Argentina (20,000 metric tons) and Uruguay (20,000 metric tons), with "others," including Brazil (with 64.81 metric tons), comprising the remainder. Cooked and canned beef imports are not subject to the TRQ.

---

[22] "Livestock, Dairy and Poultry Outlook," *Economic Research Service, U.S. Department of Agriculture*, December 24, 2002. Website available at: http://www.ers.usda.gov.

[23] "World Beef Trade Overview", *Foreign Agricultural Service, U.S. Department of Agriculture*, October 17, 2002. Website available at: www.fas.usda.gov/dlp/circular/2002/02-101p/beefoverview.html.

[24] U.S. Department of Commerce, Bureau of the Census.

In July 2002, the United States announced its proposal for the WTO agriculture negotiations. The proposal specifies ambitious reform goals and reduction commitments outlined in a two-phase process for trade reform. The first phase eliminates export subsidies and reduces worldwide tariffs and trade-distorting domestic support over a 5-year period. This would be accomplished by harmonizing tariffs and trade-distorting domestic support at substantially lower levels than what is currently allowed. The elimination of export subsidies would be particularly beneficial for U.S. cattle ranchers and beef exporters, as current WTO rules cap annual budgetary outlays on export subsidies and the quantity of subsidized exports, on a product-specific basis. Specific caps on the use of export subsidies were derived from export subsidy activity in the 1986-1990 period. Consequently, the EU has recourse to extensive use of export subsidies, and spent over $2 billion on export subsidies in 2000. In comparison, the United States allotted only $20 million in export subsidies in 2000.[25]

The second phase of the U.S. proposal will entail the eventual elimination of all tariffs and trade-distorting support. Key elements of the U.S. proposal include the reduction of tariffs, using a formula approach which cuts high tariffs more than low tariffs and the elimination of monopoly import control of state trading enterprises. The United States also proposes to eliminate the special agricultural safeguard as currently defined. Although WTO rules allow for the application of additional tariffs on a specific list of products when triggered by a surge of imports or a decline in price, this provision has not been used in any meaningful way. The United States has, however, identified the need for WTO members to improve import relief mechanisms for perishable and cyclical products in the context of the WTO negotiations.

It should also be noted that in the United States, federal assistance to the cattle sector is limited solely to emergency measures approved for a specific scope and period of time to address the needs of producers suffering losses due to drought, hot weather, disease, insect infestation, flood, fire, hurricane, earthquake, severe storms, or other natural disasters. Therefore, the aforementioned negotiating initiatives seek to address the market distortions created by foreign cattle and beef subsidies while protecting U.S. ranchers from unfair trade practices and increasing opportunities for U.S. beef exports.

c. Argentina

In 2002, Argentina's beef sector began its recovery from both animal health problems and a national economic and financial crisis. Following the 2001 outbreak of FMD, many traditional export markets closed, decreasing the first quarter 2002 volume of exports by 80 percent. By early 2002, Argentina had successfully controlled FMD through vaccination and

[25] Additional information on the U.S. proposal on agriculture, as well as the complete text of the U.S. submission, can be found on the website of the United States Trade Representative. Website available at: http://www.fas.usda.gov/itp/wto/proposal.htm.

exports resumed to over 40 countries.[26] The United States and Canada still remain closed to fresh, chilled, and frozen beef exports.

Argentine beef exports are forecast to increase to 360,000 metric tons in 2003, up significantly from the previous two years. The major devaluation of the Argentine currency in early 2002 has benefitted both cattle ranchers and beef processors, as cattle and beef prices have risen while input prices, with the exception of fuel and imports, have generally held steady. Although Argentina's beef imports are negligible, the United States has successfully exported sweetbreads and bovine genetics (semen) in the past. In 2002, however, Argentine officials placed new restrictions on the importation of high-risk animal products related to BSE, and prohibited the importation of U.S. sweetbreads. U.S. officials have been working with Argentina to have this prohibition lifted.

Argentina's financial difficulties have precluded the granting of any new subsidy programs to be offered to beef and cattle producers in 2002. FMD vaccinations, provided by the government for free in 2001, became the responsibility of producers in 2002.[27] While Argentina's tax rebate system has undergone several changes over the past few years, agricultural products such as beef shipped outside the Mercosur region remain eligible for certain rebates of indirect taxes or other commensurate benefits. In early 2002, the Argentine government reinstituted export taxes, and set the rate for beef products at five percent, largely offsetting any export rebates under the *Reintegro* program. Slaughterhouses continue to benefit from certain tax advantages instituted two years ago to assist targeted industries facing economic difficulties. Finally, the *Argentine Beef Promotional Institute*, created in 2001 by the Argentine Congress, began operating in 2003. The Institute is to be financed by producer levies through a checkoff system, with proceeds used for the promotion of beef products in both domestic and export markets.

d. Australia

As Australia's cattle herds return to record numbers not seen since the 1970's, its beef exports are expected to increase by 1.5 million tons in 2003.[28] While the United States is the largest export market for Australian beef, the TRQ limits import growth opportunities.

---

[26] "Argentina Livestock and Products Annual," Global Agricultural Information Network Report #AR2050, *United States Department of Agriculture, Foreign Agricultural Service*, September 5, 2002.

[27] "Argentina Livestock and Products, Foot and Mouth Tests Negative," Global Agricultural Information Network Report #AR2034, *United States Department of Agriculture, Foreign Agricultural Service*, June 12, 2002.

[28] "World Markets and Trade," *Foreign Agricultural Service, U.S. Department of Agriculture,* October 24, 2002. Website available at http://www.fas.usda.gov/dlp/countrypages/asbfsit.html

Australia filled its allotment in 2001 and, due to continued high level of beef shipments, is expected to fill the TRQ allotment again in 2002 and 2003.

In November 2002, USTR notified Congress of the Administration's intent to enter into negotiations with Australia on the establishment of a Free Trade Agreement. From the outset, USTR and the SEO have recognized the important role agricultural issues play in these negotiations and the potential impact of an FTA on the cattle and beef industries in particular.

As noted in previous SEO reports to Congress, Meat and Livestock Australia (MLA), a producer levy-funded entity established by Australian law, continues to be responsible for both meat and livestock promotion and research. MLA provides R&D funding to research organizations and consultants to undertake R&D activities on behalf of MLA. Furthermore, MLA provides financial support to the Joint Livestock Export program. That program is operated jointly by MLA and LiveCorp Ltd., and conducts marketing, trade support and research activities for the livestock export trade. MLA also offers financial assistance via its *Producer Initiated Research and Development* program. This program was designed to allow Australian red meat producers to be more involved in R&D and has aided over 200 producer groups over the past ten years.[29] In 2002, MLA worked with the Australian government to develop a national identification scheme that will provide for traceability and may enhance export opportunities. The system will be administered by a joint industry-government initiative.[30] Additionally, reports indicate that MLA received A$5 million ($2.78 million) in direct funding from the Australian government to help export sales to Japan recover following its BSE crisis.

The OECD reports that Australia instituted a certification regime in late 2001 for all imported beef products and now requires that all beef sold in Australia must be derived from cattle that are BSE free. They also note that while Australia's overall support to agriculture is among the lowest of all OECD Members, as measured by the Producer Support Estimate (PSE) percentage, a generally available *Diesel Fuel Rebate Scheme* provides grants that reduce the cost of on-road transport to regional and rural areas.[31]

e. Brazil

---

[29] For additional information on Meat and Livestock Australia, *see* the MLA website at http://www.mla.com.au/content.cfm?sid=915

[30] Communication with U.S. Foreign Agricultural Service staff, Australia, November 14, 2002.

[31] According to the OECD, the PSE "is an indicator of the annual monetary value of gross transfers from consumers and taxpayers to agricultural producers, measured at the farm-gate level, arising from policy measures that support agriculture, regardless of their nature, objectives or impacts on farm production or income." *See*, "Agricultural Policies in OECD Countries 2002: Monitoring and Evaluation," *Organization for Economic Cooperation and Development*, 2002, pg. 78 and 236.

With a herd size of 165 million head, Brazil maintains the largest commercial cattle stocks in the world, and is now the third-largest exporter of beef, behind the United States and Australia.[32] Despite a severe economic downturn in 2002, Brazil's livestock sector experienced record production. Beef production is forecast to increase by 2.7 percent in 2003 as higher yields have been obtained by Brazilian livestock producers, resulting in an increased calf crop, and improved weather conditions facilitate continued growth.[33] Although exports of fresh beef to the United States are still prohibited due to animal health issues, the rapid devaluation of the Brazilian real in 2002 will have a significant impact on exports to other markets in the year ahead.[34] Additionally, exports of canned, processed, and dried beef products to the United States, which are not subject to TRQ or FMD restrictions, are expected to continue growing in 2003.

Almost three quarters of Brazil's cattle herd is now free of FMD, and the entire country is expected to be FMD-free by 2005, with vaccination.[35] Brazil has sought to work with animal health officials from the United States to gain approval for individual states that are FMD-free to begin exporting fresh, chilled, or frozen beef to the United States. Regional FMD-free status was accepted by several countries in 2002, including Egypt, Russia, and China.

The FAS reports that the Brazilian government continues to maintain many of the subsidy programs to its cattle industry identified in previous SEO reports to Congress. This year, Brazilian cattle producers took greater advantage of the *Program for Pasture Improvement* (PROPASTO), which was created by the federal government in 2000. For 2003, $120 million has been allocated to this program. Cattle producers can use subsidized interest rates provided by this program to improve forage seed production. It allows each livestock producer to borrow up to R$150,000 (US$50,000) with a fixed subsidized below market interest rate. The program is expected to further increase beef production by 10 percent, or 220,000 metric tons.

The *SOLO/WAREHOUSE* program assists livestock producers wishing to build or rebuild their silos and warehouses on their farms. The program has been allocated a total budget of $33 million in the 2002/2003 crop year. Producers can borrow up to $33,000 each in fixed-term below-market interest rate loans. The *MODERFROTA* program assists farmers in modernizing their agricultural machinery. With a total allocation of R$1 billion (US$333 million), the program lends to livestock producers who earn up to R$250,000

---

[32] "Where's the Beef From? Increasingly, the Answer is Brazil," by Miriam Jordan, *Wall Street Journal,* April 1, 2002. pg. A9.

[33] "Brazil Livestock and Products Annual," Global Agricultural Information Network Report #BR2610, *United States Department of Agriculture, Foreign Agricultural Service*, August 26, 2002, pg. 1-2.

[34] *Id.*, at 1.

[35] *Id.*, at 1-2.

(US$83,000) annually. The loans are for 100 percent of the purchase price of machinery and may be financed at a fixed, below-market interest rate. However, producers above that income ceiling may still finance agricultural machinery up to 90 percent of the purchase price.[36]

The *FINAME* program, offered through the National Bank for Economic and Social Development (BNDES), continues to benefit cattle producers in Brazil. Benefits under the program include subsidized long term loans for both seeds and breeding programs.[37] BNDES also sponsors other programs used by meat packers which may help finance beef exports. The ACC and ACE programs under BNDES allow exporters to lower costs of exportation. Through these programs, exporters can obtain a cash advance based on an export contract either before or after shipment, depending on the program selected. The *BNDES-Exim* program, also known as the *Brazilian Eximbank*, is designed to expand Brazilian exports generally by providing lines of credit to exporters.

The Brazilian Beef Processors and Exporters Association (ABIEC), which is comprised of the largest beef processors, packers, and exporters, has initiated an aggressive marketing promotion program that was first described in our 2002 report. The objective of the program is to promote the brand "Brazilian Beef," and ABIEC's budget for market promotion (estimated at U.S. $2.2 million) is 50 percent funded by the National Export Promotion Agency.[38]

In addition to federally-sponsored programs, various states and municipalities also offer programs potentially beneficial to cattle and beef producers, such as state tax incentives and pasture recuperation programs. Moreover, some states are trying to promote their own brands similar to the "Brazilian Beef" program.

f. China

There are several government programs in existence that are beneficial to the stock raising industry in China. First, in 2001, the government announced that it will increase its input for infrastructure related to cattle production, with a goal of having it account for more than 10 percent of total agriculture infrastructure input. Additionally, as part of the West Development Program, cattle feedlots in Shaanxi and Gui Zhou provinces enjoy a beneficial 15 percent enterprise income tax rate from 2001 to 2010. Second, reports indicate that the Chinese government plans to launch a national program aimed at enhancing the competitiveness of the farming industry. The program will concentrate resources on

---

[36] "Brazil Livestock and Products Annual," Global Agricultural Information Network Report #BR2610, *United States Department of Agriculture, Foreign Agricultural Service*, August 26, 2002, pg. 4.

[37] *Id.*

[38] *Id.*

developing nine different farming zones that are highly specialized in processing specific products, including a beef and mutton belt in central China.[39] Finally, there have not been any changes to previously identified programs, including the World Bank funded feedlot and capacity-building program first identified in 2001.

As demand for beef increases in China, imports are expected to grow. The U.S. FAS reports that U.S. exports to China grew strongly in 2002, with muscle meat exports surpassing offal exports for the first time.[40] The United States supplies the largest portion of Chinese beef imports by a large margin over Australia and New Zealand. Tariff reductions scheduled for 2003 and 2004 will also foster additional export growth opportunities for U.S. beef products. Chinese beef exports are expected to decline in 2002 and 2003 due to economic factors in Hong Kong and food safety concerns related to Chinese products. Other export markets for Chinese beef include Russia, Kuwait, and Egypt.

g. European Union

In 2002, the European cattle and beef industry began to recover from the severe animal health crisis of 2001. While over 180,000 head of cattle were found to be contaminated with BSE in the EU as of June 2002, new testing requirements and animal health regulations boosted consumer confidence and augmented weakened demand for beef products.[41] By February 2002, the United Kingdom (UK) became the last EU Member to achieve FMD disease-free status. The crisis also fostered a series of new labeling requirements that first went into effect in 2000, and were strengthened in early 2002 to include identification of the country of birth and country where the animal was fattened.[42] Bringing FMD and BSE under control also boosted both exports and imports, with further increases expected in 2003. U.S. red meat exports to the EU remain subject to non-hormone treated conditions, listing requirements and mandatory residue monitoring.

On the broad policy front, the European Commission tabled its mid-term review of the EU's Common Agricultural Policy (CAP) in 2002. The Commission reported that public expenditure for the farm sector must be better justified. Their review proposes cutting the link between production and direct payments; making those payments conditional to environmental, food safety, animal welfare and occupational safety standards; substantially

---

[39] "China Looking To Boost Output Of Processed Agricultural Products," *Inside U.S. Trade's ChinaTradeExtra.com*, August 19, 2002.

[40] "China Livestock Annual Report," Global Agricultural Information Network Report #CH2044, *United States Department of Agriculture, Foreign Agricultural Service*, September 15, 2002.

[41] European Union Livestock and Products Annual," Global Agricultural Information Network Report #E22091," *United States Department of Agriculture, Foreign Agricultural Service*, September 24, 2002.

[42] For additional information on the EU's country of origin labeling policies, see, "Identification and Labeling of Beef and Veal" at: http://europa.eu.int/scadplus/leg/en/lvb/l12064.htm

increasing EU support for rural development; and instituting new rural development measures to boost quality production, food safety, and animal welfare, and to cover the costs of a new farm audit system.[43] In December, European officials announced their proposal for the WTO agricultural negotiations. Key elements include cutting import tariffs by 36 percent, export subsidies by 45 percent (as opposed to the United States' proposal to totally eliminate export subsidies) and reducing trade-distorting domestic farm support by more than half.[44] Finally, the European Union completed negotiations with 10 applicant countries for EU membership beginning in 2004. The SEO will closely monitor how CAP reforms proceed and how CAP assistance is phased in for those new Members, and what effect these changes may potentially have on cattle and beef trade both within Europe and around the world.

The SEO, working with FAS staff overseas, has identified a number of Community-wide programs that potentially benefit the cattle and beef sectors. Information on several of these subsidy programs was included in previous reports to Congress. In its 2002 Report, the OECD notes that beef in the EU is still "supported through intervention prices, intervention purchases, headage payments based on fixed reference livestock numbers subject to limits on stock density, tariffs, TRQs and export subsidies."[45] The FAS reports that the 2002 EU budget for the beef sector should exceed €7,580 million, amounting to 17 percent of the entire agricultural budget.[46]

The following Community-wide programs were reported by the FAS to benefit cattle-raising operations, slaughterhouses, and traders in 2002[47]:

- *Suckler Cow Premia*: €1,977 million, a small increase over 2001.
- *Special Premia on Cows and Bulls:* €1,788 million, a small increase over 2001.
- *Slaughter Premia:* €1,184 million.
- *Extensification Premia (for extensive production of 13.7 million head):* €891 million.

---

[43] For additional information on the EU's Common Agricultural Policy and efforts aimed at reform, *see*, http://europa.eu.int/comm/agriculture/mtr/index_en.htm

[44] "WTO and Agriculture: European Commission proposes more market opening, less trade distorting support and a radically better deal for developing countries." *Press Release of the European Commission*, December 16, 2002. Website available at: http://europa.eu.int/comm/agriculture/index_en.htm

[45] "Agricultural Policies in OECD Countries 2002: Monitoring and Evaluation," *Organization for Economic Cooperation and Development*, 2002, pg. 88-93.

[46] "European Union Livestock and Products EU 2002 Beef Sector Subsidies," Global Agricultural Information Network Report #E22109, *United States Department of Agriculture, Foreign Agricultural Service*, November 15, 2002.

[47] *Id.*

- *Export Refunds:* €488 million, a decrease from 2001 due to low prices.
- *Storage Costs for Intervention Stocks:* €466 million, with the last intervention scheme (Special Purchase Scheme) discontinued in March 2002. Low prices triggered the purchase of approximately a quarter of a million metric tons of beef, which are slowly being sold on the market as demand rises. Intervention schemes have now been fully replaced by the *Aid for Private Storage* scheme. Under this program, a payment is made by the EU to traders who agree to store beef at their own expense for a specific amount of time, during which time the beef is effectively removed from the market. After the storage period ends, the beef remains under the ownership of the private party rather than the government.
- *Slaughter of Bovines Over 30 Months:* €390 million, as part of the measures related to BSE in the UK. An additional €75 million are available for compulsory slaughter programs when BSE cases are detected elsewhere.
- *Other Measures*: €322 million are available as additional payments granted by Member states according to their own priorities.

h. Japan

In Japan, the government responded to a deterioration in demand for beef following the confirmation of its first case of BSE in 2001. An additional case of BSE was detected in May, and Japanese officials estimate total industry-wide damage at up to $3 billion.[48] Consumers remained cautious and overall beef consumption was down 20 percent at mid-year, with only a gradual recovery predicted.

The United States continues to be the major exporter of beef products to Japan, although imports of U.S. frozen beef fell approximately 25 percent due to the adverse market conditions. As demand rebounds, Australia will continue to provide the most competition for the Japanese import market. U.S. exports may also be impacted by the imposition of a safeguard mechanism, which is designed to boost the import tariff if imports exceed a trigger level of 117 percent of the previous year's imports. Thus, a return to historic levels for U.S. exports in 2003 may trigger the safeguard due to the low import levels in the first quarter of 2002.

In February, the government began purchasing up to 70,000 beef cattle for $376 per head. Meat processing firms were eligible for a subsidy of $75 per head for each government purchased cow processed. The processed beef was to be sold on the domestic market or incinerated, depending on demand. The program, with a budget of $150 million, is set to expire in February, 2003.[49] Consumer confidence in domestic beef was further

---

[48] "Japan Confirms New Mad Cow Case," *Cable News Network*, CNN.com, May 13, 2002.

[49] Associated Press Newswire, *Associated Press*, January 31, 2002. *See* also: "BSE... Costly Competition in Japan," *AGRI-NEWS*, February 22, 2002, pg. 14.

eroded when major domestic processors were accused of using pork and imported beef to claim the subsidy. The BSE scare also led Japan to institute a program to identify all of the beef cattle in the country. Finally, the OECD reports that guaranteed prices for calves per head remained unchanged (at 131,000 Japanese yen) in 2001/02 from their 2000 levels.[50]

i. New Zealand

New Zealand exports eighty percent of its beef production.[51] Sixty-four percent of those exports enter the U.S. market, and an additional ten percent are exported to Canada.[52] As of mid-2002, New Zealand had already filled 60 percent of its U.S. TRQ of 213,402 tons.[53] However, exports have slowed and, through October 2002, U.S. imports of fresh and chilled meat are down approximately 9 percent compared to imports in 2001.[54]

The OECD reports that New Zealand's overall support to agriculture, as measured by the PSE, has been one percent since 1998 and continues to be the lowest among OECD Members.[55] New Zealand made its most recent submission to the WTO on its subsidy programs on December 18, 2002. The report does not indicate any changes or modifications to the programs that potentially benefit the cattle and beef industries that were identified in the 2002 SEO Report to Congress.[56] The *Sustainable Farming Fund* (SFF), which was detailed in the 2001 SEO Report is still in operation. The SFF budget was NZ$ 8.762 million in 2001/2002, and is scheduled to rise to NZ$ 9.550 million in 2002/2003.[57] The Export Credit Office of the New Zealand Treasury administers an *Export Credit Scheme* (ECS). The ECS was established in 2001 and is designed for capital goods; however, exporters of live cattle for breeding purposes are eligible for aid under this program.

---

[50] "Agricultural Policies in OECD Countries 2002: Monitoring and Evaluation," *Organization for Economic Cooperation and Development*, 2002, pg. 117.

[51] "Beef New Zealand," Statistics, Beef Exports. Website available at: http://www.beef.org.nz/statistics/sld004.asp

[52] "New Zealand Livestock and Products Annual," Global Agricultural Information Network Report #NZ2027, *United States Department of Agriculture, Foreign Agricultural Service*, September 5, 2002, pg. 8.

[53] *Id.*

[54] U.S. Department of Agriculture, Foreign Agricultural Service, FAS Agricultural Import Commodity Aggregations. Website available at: http://www.fas.usda.gov/ustrdscripts.

[55] "Agricultural Policies in OECD Countries 2002: Monitoring and Evaluation," *Organization for Economic Cooperation and Development*, 2002, pg. 128.

[56] "New and Full Notification Pursuant to Article XVI:1 of the GATT 1994 and Article 25 of the Subsidies Agreement," New Zealand, (G/SCM/N/71/NZL), December 19, 2002.

[57] Communication with U.S. Foreign Agricultural Service staff, New Zealand, November 19, 2002.

j. Republic of Korea

In 2002, the United States remained the dominant supplier of beef to the Korean market, with exports growing throughout the year. In 2003, Korea's overall beef imports are expected to reach a record 420,000 metric tons, due primarily to rising demand, a substantially smaller domestic cattle herd, and the continuing positive effects of Korea's 2001 liberalization of retail sales barriers.[58] Korea also imports beef from Australia, Canada, and New Zealand, and exports neither beef nor live cattle. The May 2002 outbreak of FMD had only a minor impact on domestic beef production and consumption, as the disease mostly affected swine rather than cattle.

The OECD reports that approximately half of Korea's cattle operations participated in a calf breeding stabilization scheme, which covered 348,000 cows and provided a maximum deficiency payment of $194 per calf.[59] The FAS identified several programs administered by the Korean Ministry of Agriculture and Forestry (MAF) aimed at stimulating greater on-farm retention of breeding stock and calf production to stabilize the national herd size and increase the cow/calf ratio.[60] The *Project for Stabilization of Calf Production* establishes a market floor price (minimum standard price) for calves at 1.2 million won per head. The program pays participants the difference between the market price at the time of sale and a market floor price (up to 250,000 won per calf). The program budget in 2002 was approximately $51 million (60,097 million won).

The *Establishment of Calf Production Base* program is designed to encourage development of larger farm operations devoted to cow/calf production. In 2002, the MAF sought to establish 10 such farms, each with at least 20 hectares of grassland. The 2002 budget was approximately $4.8 million.

The *Subsidy for Multi-production of Hanwoo Beef Cattle* is also designed to encourage the retention of Hanwoo breeding stock. Incentives rise based on the number of live-Hanwoo calf births from individual cows. Producers are paid approximately $168 dollars for the third and fourth calf born to a cow, and the subsidy grows to approximately $252 for the fifth calf born to the same cow. The total 2002 budget for this program was $20.7

---

[58] "World Beef Trade Overview", *Foreign Agricultural Service, U.S. Department of Agriculture*, October 17, 2002. Website available at: www.fas.usda.gov/dlp/circular/2002/02-101p/beefoverview.html.

[59] "Agricultural Policies in OECD Countries 2002: Monitoring and Evaluation," *Organization for Economic Cooperation and Development*, 2002, pg. 119.

[60] Information on the Ministry of Agriculture and Forestry subsidy programs included in this report was compiled by FAS staff in Korea. *See*, "Korea, Republic of, Livestock and Products, Annual 2002, Global Agricultural Information Network Report #KS2044," *United States Department of Agriculture, Foreign Agricultural Service,* September 6, 2002. *See, also* Report #KS2005, February 1, 2002.

million. Over 113,000 calves had received benefits during the period of January - June 2002.

Finally, the MAF administers the *Hanwoo Integrated Measures Program*, which is designed to improve the quality of Hanwoo beef. Producers receive a subsidy of $150 per head for each Hanwoo bull castrated. The 2002 program budget was approximately $14.1 million.

k. Conclusion

Cattle and beef trade continued to evolve as production and consumption patterns changed throughout the world. In 2002, government assistance programs remained available to cattle and beef producers in all the major beef-producing countries. While not all of these programs necessarily distort trade and damage the prospects of U.S. producers and exporters, they do affect an increasingly interdependent world market for beef. Reporting on these programs fulfills our mandate to ensure that both U.S. trade negotiators and Members of Congress are aware of the programs in existence in this sector. In 2003, the SEO will continue to closely monitor each of these practices, and work to identify new subsidy programs, so that those responsible for the ongoing WTO agricultural negotiations and free trade agreements to be pursued in the year ahead have a complete understanding of the scope of government activity in the cattle and beef industry.

B. DEFENDING U.S. INTERESTS IN WTO DISPUTES BROUGHT BY OTHERS

1. Foreign Sales Corporation Tax Rules

In November 1997, the EU requested consultations with the United States with respect to the Foreign Sales Corporation (FSC) provisions of U.S. tax law (sections 921-927 of the Internal Revenue Code), claiming that these rules constituted a subsidy inconsistent with U.S. obligations under both the WTO Subsidies and Agriculture Agreements. The FSC provisions provided exporters with a partial tax exemption on certain foreign income of "foreign sales corporations," which typically were foreign subsidiaries of U.S. companies. Following consultations, a dispute settlement panel was formed and the panel issued its report on October 8, 1999, finding that the tax exemption conferred by the FSC provisions constituted a prohibited export subsidy under the Subsidies Agreement. The panel also found that the tax exemption constituted an export subsidy which violated U.S. export subsidy commitments under the Agriculture Agreement. With respect to the panel's findings under the Subsidies Agreement, the panel recommended that the United States withdraw the FSC tax exemption "with effect from" October 1, 2000.

On November 26, 1999, the United States appealed the panel's findings, and, subsequently, the EU also appealed the panel's resolution of certain issues. The Appellate Body circulated its report on February 24, 2000. The Appellate Body upheld the panel's

finding that the FSC tax exemption constituted a prohibited export subsidy under the Subsidies Agreement, although its reasoning differed somewhat from that of the panel. The Appellate Body reversed the panel's finding that the FSC tax exemption fell under Article 9.1(d) of the Agriculture Agreement. However, the Appellate Body found that the FSC tax exemption nonetheless was an "export subsidy" within the meaning of Article 1(e) of the Agriculture Agreement which resulted in, or which threatened to lead to, circumvention of U.S. export subsidy commitments with respect to both scheduled and unscheduled agricultural products.

The DSB adopted the panel and Appellate Body reports on March 20, 2000. On April 7, the United States informed the DSB of its intention to implement the recommendations and rulings in a manner which respects U.S. WTO obligations. Throughout the spring and summer of 2000, the executive branch worked with Congress and the private sector to develop legislation which would: (1) repeal the FSC provisions; and (2) provide tax treatment for foreign sales similar to that afforded by territorial-type tax regimes, such as are found in Europe. The United States consulted with the EU as the legislation was being developed, and the EU made known that it would challenge the WTO consistency of the legislation being developed. As a result, in order to avoid further escalation of bilateral tensions, the United States and the EU agreed on September 29, 2000 on procedures to govern any EU challenge to the FSC replacement legislation. The agreement essentially provided that the WTO consistency of the replacement legislation be resolved before considering questions relating to what, if any, countermeasures might be imposed by the EU.

After it became apparent that the United States would be unable to meet the October 1 deadline, the United States requested, and the DSB agreed, to extend the deadline to November 1, 2000. On November 15, the United States enacted the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (the ETI Act). The ETI Act repealed the FSC provisions and established a new regime under which extraterritorial income – as defined in the Act – is not subject to tax.

On November 17, under Article 21.5 of the DSU and in accordance with the U.S./EU procedural agreement, the EU requested dispute settlement consultations with respect to the ETI Act. On the same day, and also in accordance with the procedural agreement, the EU requested authority from the DSB to take countermeasures and suspend concessions in the amount of $4.043 billion per year. On November 27, the United States objected to the appropriateness of the countermeasures and the level of suspensions proposed by the EU, thereby resulting in the referral of the matter to arbitration.

Following consultations, the EU on December 7 requested the establishment of a dispute settlement panel to review the compatibility of the ETI Act with WTO obligations. On December 20, the DSB established a panel under Article 21.5 of the DSU to consider the EU's claims regarding the WTO consistency of the ETI Act. The panel was composed of the three panelists from the original proceeding. On December 21, the United States and the EU, in accordance with the procedural agreement, jointly requested that the arbitrators (also

the three original panelists) suspend the arbitration proceedings until the adoption of the panel report or, in the event of an appeal, the Appellate Body report in the Article 21.5 proceeding.

The panel circulated its final report on August 20, 2001. The panel found the ETI Act to be inconsistent with U.S. obligations under the WTO in the following respects: (1) the panel found that the ETI Act's tax exclusion constitutes an export subsidy that is prohibited by the Subsidies Agreement and that is inconsistent with U.S. export subsidy commitments under the Agriculture Agreement; (2) the ETI Act's 50 percent foreign value rule is inconsistent with Article III:4 of GATT 1994; and (3) the ETI Act's transition rules are inconsistent with the DSB's recommendation to withdraw the FSC subsidy with effect from November 1, 2000.

On October 15, 2001, the United States appealed the panel's findings, and, subsequently, the EU also appealed the panel's resolution of certain issues. On January 14, 2002, the Appellate Body affirmed the findings of the panel, although its reasoning differed from that of the panel. The DSB adopted the panel and Appellate Body reports on January 29, 2002.

In accordance with the U.S./EU procedural agreement, the adoption of the reports triggered the resumption of the arbitration proceeding. The arbitration decision was circulated on August 30, 2002, and the arbitrator found that the countermeasures proposed by the EU were "appropriate" within the meaning of Article 4.10 of the Subsidies Agreement. To date, however, the EU has not sought final authorization from the DSB to impose countermeasures.

In the meantime, President Bush expressed his intention to work with Congress to fully comply with the DSB's recommendations. To that end, the Administration has been participating in a bicameral, bipartisan Working Group on the development of WTO consistent legislation to replace the FSC/ETI provisions.

2. "Privatization" or "Change-in-Ownership" Countervailing Duty Methodology Disputes

On June 30, 1998, the EU requested consultations with the United States regarding the imposition of countervailing duties on certain hot-rolled lead and bismuth carbon steel (lead bar) from the UK. *United States - Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom (DS138)*. The EU contended that the imposition of duties was based on the inappropriate treatment by Commerce of subsidies received by the government-owned British Steel Corporation (BSC). Specifically, the EU alleged that Commerce inappropriately attributed subsidies received by BSC to two private successor companies that were created as part of the 1988 privatization of BSC. Following consultations held in July 1998, a panel was established.

The focus of the dispute was on the question: "What happens to subsidies received by a government-owned company when the company is privatized?" At that time, Commerce applied a methodology known as "gamma," under which Commerce considered part of the price paid by private owners for a government-owned company to constitute repayment to the government of prior subsidies, the precise amount being determined by the application of a formula known as "gamma". In practice, this typically meant that Commerce regarded a privatized company as remaining subsidized, but to a lesser extent than it was before privatization.

The panel circulated its final report on December 23, 1999, and found that Commerce's application of the gamma methodology in the UK lead bar CVD proceeding was inconsistent with the Subsidies Agreement. According to the panel, a distinction had to be drawn between BSC – the original subsidy recipient – and the successor companies. The panel stated that the changes in ownership, which were based on the payment of full consideration for the assets of BSC, required Commerce to reexamine whether the products produced by the successor companies were subsidized. Commerce did not do this, the panel said, but instead irrebuttably presumed that the successor companies continued to benefit from the subsidies provided to BSC. The panel added that, in its view, no benefit existed on the facts of the case, because the transactions that created the successor companies were at "arm's length" and for "fair market value."

The United States appealed, and on May 10, 2000, the Appellate Body issued its report. The Appellate Body upheld the panel's findings, although its reasoning differed somewhat from that of the panel. In particular, the Appellate Body rejected the U.S. position that the benefit of a subsidy is to productive operations or the product itself, and found instead that the benefit is received by a legal or natural person. In this case, the Appellate Body said, Commerce erred by not considering whether the successor companies to BSC – the "legal persons" – received any benefit. Noting the panel's finding that the transactions in question were at arm's length and for fair market value, the Appellate Body upheld the panel's finding that the financial contributions bestowed on BSC could not be considered to confer a benefit on the successor companies. The Appellate Body emphasized, however, that its conclusions were limited to the specific circumstances of the case before it.

The DSB adopted the panel and Appellate Body reports on June 7, 2000. For the following reasons, however, no further action was required by the United States with respect to the DSB's recommendations, which were limited to the specific CVD proceeding on UK lead bar. While the panel and Appellate Body proceedings were pending, Commerce was conducting a "sunset review" of the CVD order on UK lead bar. In the course of that review, the U.S. petitioners expressed no interest in maintaining the order, and requested that the order be revoked with retroactive effect so as to cover the administrative reviews that were the subject of the WTO dispute. As a result, by the time the Appellate Body issued its report, Commerce already had revoked the order and canceled the imposition of any countervailing duties on imports covered by the contested administrative reviews. Accordingly, at the DSB meeting on July 5, 2000, the United States stated that no further action was necessary to implement the recommendations of the DSB.

Nevertheless, while the WTO dispute was ongoing, there was a significant domestic legal development. On February 2, 2000, the Court of Appeals for the Federal Circuit (CAFC) found Commerce's privatization or "change of ownership" methodology to be inconsistent with U.S. law. This case – *Delverde, SRL v. United States*, 202 F.3d 1360 – involved a transaction between two private firms, but the methodology employed by Commerce was essentially the same as the gamma methodology it used to examine the privatization of government-owned firms. Although the CAFC did not rely on the WTO panel report as authority, the CAFC did state that the panel report was "not inconsistent with our holding."

The CAFC subsequently denied Commerce's request for a rehearing by the entire court, and the Administration at the time declined to seek further review by the U.S. Supreme Court. Accordingly, Commerce began the process of reexamining its privatization and change of ownership methodologies in light of the *Delverde* decision. As part of this process, Commerce requested remands from the Court of International Trade (CIT) in those cases where these methodologies were at issue in order to allow Commerce to make revised determinations consistent with the CAFC's decision.

On November 10, 2000, the EU requested dispute settlement consultations with respect to 14 outstanding U.S. CVD orders involving imports from various EU member states in which there was a change-in-ownership issue. *United States - Countervailing Measures Concerning Certain Products from the European Communities (DS212)*. The gist of the EU claim was that the imposition of countervailing duties in these cases was invalid to the extent that Commerce continued to rely on the gamma methodology that had been the subject of the earlier WTO dispute settlement proceeding. Consultations were held on December 7, 2000.

In addition, on December 21, 2000, Brazil requested dispute settlement consultations with respect to Commerce's privatization methodology. The two U.S. CVD measures cited in the consultation request were sunset review determinations involving the CVD order on cut-to-length plate from Brazil and the suspended investigation on certain hot-rolled steel from Brazil. Consultations were held on January 17, 2001.

Shortly after the EU consultation request, however, Commerce issued draft redeterminations in four of the cases in which it had obtained remands from the CIT. In these redeterminations, Commerce applied a revised methodology, which came to be known as the "same person" methodology. Under the same person methodology, Commerce first asked whether the producer/exporter of the subject merchandise was the same legal person that had received a subsidy prior to a privatization or change in ownership. If it was, Commerce determined that the producer/exporter was the same person and, accordingly, continued to benefit from the original subsidies. If, on the other hand, the pre-sale and post-sale entities were determined to be different legal persons, Commerce would find no continuing benefit from the original subsidies, but instead would have analyzed whether a new subsidy had been provided to the post-sale entity through the particular privatization/change-of-ownership transaction in question. In each of the four

redeterminations made in response to remands from the CIT, Commerce found the post-sale entity to be the same legal person and, therefore, found that the benefit of the original subsidies continued.

The EU requested a further round of consultations to consider, among other things, Commerce's new same person methodology. Consultations were held on April 3, 2001.

On August 8, 2001, the EU requested the establishment of a dispute settlement panel with respect to 12 of the 14 CVD proceedings identified in its original consultation request. In addition to challenging the continued application of the gamma methodology and the new same person methodology, the EU also challenged the WTO consistency of section 771(5)(F) of the Tariff Act of 1930, the provision of the CVD statute that specifically deals with the change-of-ownership issue. The DSB established a panel on September 10, with Brazil, India and Mexico reserving their right to participate as third parties.

The panel circulated its final report on July 31, 2002. The panel found in favor of the EU with respect to all of its claims. According to the panel, the sale of a firm at arm's length and for fair market value creates an irrebuttable presumption that prior subsidies are extinguished. The panel found that each of the 12 Commerce determinations at issue reached results that were inconsistent with this presumption. The panel also found section 771(5)(F) to be WTO inconsistent because, according to the panel, it precluded Commerce from applying the panel's irrebuttable presumption.

The United States appealed, and the Appellate Body issued its report on December 9, 2002. The Appellate Body rejected the panel's irrebuttable presumption, and found instead that an arm's length, fair market value sale of a firm merely creates a *rebuttable* presumption that prior subsidies are extinguished. Therefore, the Appellate Body reversed the panel's finding concerning section 771(5)(F), because that finding was based on the panel's erroneous notion of an irrebuttable presumption.

However, the Appellate Body upheld the panel's findings regarding Commerce's methodology, although its reasoning again differed somewhat from that of the panel. With respect to the same person methodology, the Appellate Body rejected the panel's position that there is never any distinction between a firm and its owners. However, it also rejected Commerce's position that a firm and its owners are always completely separate. According to the Appellate Body, to adequately determine whether a privatized firm continued to benefit from pre-privatization subsidies, Commerce had to do more than merely ask whether a new legal person was created. Thus, the Appellate Body found that the same person methodology, as such and as applied, is inconsistent with the Subsidies Agreement.

The DSB adopted the panel and Appellate Body reports on January 8, 2003. As of this writing, the United States has yet to inform the DSB of its intentions regarding implementation of the DSB's recommendations.

However, as in the first panel proceeding involving UK lead bar, there have

been significant domestic legal developments. On January 4, 2002, Judge Barzilay of the CIT issued two decisions in which she held that the same person methodology is inconsistent with the U.S. CVD statute, as interpreted by the CAFC in *Delverde*. The CIT remanded the agency determinations in question – both of which were the subject of the WTO dispute – to Commerce for redeterminations consistent with the court's opinion. The two CIT decisions are *Allegheny Ludlum Corp. v. United States*, 182 F. Supp. 2d 1357, and *GTS Industries S.A. v. United States*, 182 F. Supp. 2d 1369.

Subsequently, on February 1, 2002, Judge Wallach of the CIT also ruled against the same person methodology in *Acciai Speciali Terni S.p.A. v. United States*, Slip Op. 2002-10, 2002 Ct. Intl. Trade LEXIS 25. On March 29, 2002, Judge Goldberg of the CIT ruled against the methodology in *ILVA Lamiere E Tubi S.R.L. v. United States*, 196 F. Supp. 2d 1347.

However, on June 4, 2002, Chief Judge Carman of the CIT upheld Commerce's use of the same person methodology in *Acciali Speciali Terni S.p.A. v. United States*, 206 F. Supp. 2d 1344. As of this writing, the decisions of Chief Judge Carman and Judge Barzilay have been appealed, and the privatization issue is once again before the CAFC.

3. EU's Challenge of the Countervailing Duty Review of Certain Corrosion-Resistant Carbon Steel Flat Products from Germany

In addition to its consultation request concerning the privatization issue, on November 10, 2000, the EU also requested dispute settlement consultations with the United States concerning the outcome of a sunset review of the CVD order on certain corrosion-resistant carbon steel flat products from Germany (German Steel case). Consultations were held on December 8, 2000.

Initially, the crux of the EU complaint appeared to be that the United States does not apply the one percent *de minimis* subsidy standard of Article 11.9 of the Subsidies Agreement to the sunset review phase of CVD proceedings, but instead, by regulation, applies a *de minimis* standard of 0.5 percent. The U.S. position is that Article 11.9, by its terms, is limited to the investigation phase of a CVD proceeding and that the Subsidies Agreement does not impose any *de minimis* standard for the sunset review phase.

On February 5, 2001, the EU filed a second request for consultations. In this second request, the EU expanded its claims to include general and case-specific allegations regarding certain basic aspects of U.S. procedures for sunset reviews, including the U.S. statutory requirement that Commerce self-initiate sunset reviews in all cases. Consultations were held on March 21, 2001.

On August 8, 2001, the EU requested the establishment of a dispute settlement panel. The panel circulated its final report on June 14, 2002, making the following findings in favor of the United States: (1) the panel found that the EU's claims regarding the Commerce system of "expedited sunset reviews" was not within the panel's terms of reference; (2) the panel found that the EU's claims regarding "ample opportunity" for parties

to submit evidence in a sunset review were not within the panel's terms of reference; (3) the U.S. system of automatically initiating sunset reviews is not inconsistent with the Subsidies Agreement; (4) Commerce's self-initiation of a sunset review in the German Steel case was not inconsistent with the Subsidies Agreement; and (5) the U.S. CVD law, as such, is not inconsistent with the Subsidies Agreement with respect to the obligation of investigating authorities to "determine" in a sunset review the likelihood of a continuation or recurrence of subsidization.

However, the panel did make the following findings against the United States: (1) the panel found that in the German Steel case, Commerce's determination of likelihood of a continuation or recurrence of subsidization lacked a "sufficient factual basis" and, therefore, was inconsistent with Article 21.3 of the Subsidies Agreement; (2) the panel found (with a dissent) that the U.S. CVD law, as such, is inconsistent with the Subsidies Agreement because it does not apply the 1 percent *de minimis* standard of Article 11.9 to sunset reviews; and (3) the panel found (again with a dissent) that Commerce acted inconsistently with the Subsidies Agreement by failing to apply a 1 percent *de minimis* standard in the German Steel sunset review.

The United States appealed the panel's findings concerning the *de minimis* issue, but did not appeal the panel's case-specific finding concerning Commerce's determination of likelihood. The EU, in turn, filed an appeal with respect to most of the panel's findings that were adverse to the EU. The United States appeal focused, in particular, on the fact that the panel's findings concerning the *de minimis* issue essentially rewrote the text of the Subsidies Agreement.

The Appellate Body issued its report on November 28, 2002. The Appellate Body found in favor of the United States across the board, upholding the panel's findings that were adverse to the EU, and reversing the panel's findings regarding the *de minimis* issue.[61]

The DSB adopted the panel and Appellate Body reports on December 19, 2002. On January 17, 2003, the United States informed the DSB that it intended to implement the DSB's recommendation concerning the one adverse panel finding that the United States had not appealed.

As in the case with of disputes, there were domestic legal developments while the WTO dispute was pending. On February 28, 2002, Judge Restani of the CIT remanded the German Steel sunset review to Commerce, finding that Commerce had committed a variety of legal errors. *AG Dillinger v. United States*, 193 F. Supp. 2d 1339. Following a remand redetermination by Commerce, on September 5, 2002, Judge Restani remanded the case again to Commerce. *AG Dillinger v. United States*, Slip Op. 2002-107, 2002 Ct. Intl. Trade LEXIS 107. As of this writing, the litigation is still pending.

---

[61] The Administration believes that the Appellate Body report in this dispute serves as a model for how panels should approach interpretation of the Subsidies Agreement and other WTO agreements.

4. Section 129(c)(1) of the Uruguay Round Agreements Act

On January 17, 2001, Canada requested consultations with the United States regarding Section 129(c)(1) of the URAA, and the accompanying Statement of Administrative Action (SAA) at page 1026 of the SAA, alleging that this provision precludes the United States from complying fully with rulings of the WTO Dispute Settlement Body in cases where the United States has acted inconsistently with its WTO obligations with respect to an AD or CVD proceeding. The United States and Canada held consultations in March 2001, and a panel was established at Canada's request in August 2001. On June 12, 2002, the Panel issued a report rejecting Canada's challenge. The Panel agreed with the United States that Canada had misinterpreted section 129(c)(1) and found that the provision does not breach any of the WTO provisions that Canada had cited. The Panel refused Canada's request to issue legal findings on the nature of a Member's implementation obligations in WTO cases involving AD and CVD measures, since section 129(c)(1) did not implicate any entries of merchandise that would be affected by such issues. Canada did not appeal.

5. Canada's Challenge of Preliminary Determinations with Respect to Softwood Lumber

On August 9, 2001, the Commerce Department made an affirmative preliminary CVD determination and an affirmative preliminary critical circumstances determination with respect to softwood lumber from Canada. On August 21, 2001, Canada requested WTO consultations with the United States, alleging that the Commerce Department's determinations, as well as provisions of U.S. law governing reviews of final CVD orders, were inconsistent with various provisions of the Subsidies Agreement and GATT 1994. Following U.S.-Canadian consultations in September, the DSB established a panel on December 5, 2001. Japan, the EU, and India reserved their third party rights.

The panel released its report on September 27, 2002. The panel found in favor of the United States on two key issues. Most importantly, the panel agreed with the United States that the Canadian provincial governments' sale to lumber producers of timber from public lands constitutes a "financial contribution" by the government that can give rise to a subsidy under the terms of the Subsidies Agreement. Canada has long argued that the governments' sale of a natural resource does not fall within the disciplines of the Subsidies Agreement and therefore cannot be subject to countervailing duties under any circumstances. The panel conclusively rejected this argument.

The panel also agreed with the United States that the provisions of U.S. law governing expedited and administrative reviews of final CVD orders are consistent with U.S. obligations under the Subsidies Agreement. The panel rejected Canada's argument that U.S. laws preclude company-specific reviews in cases, like this one, where the Commerce Department calculates a country-wide rate rather than company-specific rates because of the large numbers of exporters.

The panel found against the United States with respect to the particular methodology that Commerce used to calculate the amount of the subsidy. In its preliminary determination, Commerce used prices for comparable standing timber in contiguous U.S. states as the benchmark to measure whether the government timber prices in Canada are below market, *i.e.*, provide a benefit. The Panel found that this methodology is inconsistent with the Subsidies Agreement. The Panel also found that Commerce improperly assumed that the subsidy provided to timber harvesters passed through arm's-length sales to downstream users of timber. Finally, the panel found against the United States with respect to the retroactive imposition of provisional remedies based on Commerce's preliminary determination that "critical circumstances" existed in this case. The panel found that, under the Subsidies Agreement, this remedy cannot be applied until a final determination is made. Given that the panel's report only applies to the preliminary countervailing duties, however, these findings have no impact on the final countervailing duties that are currently in effect. Canada has separately challenged the final duties at the WTO, and that proceeding is now underway.

Neither Canada nor the United States appealed the panel report. As a result, the Dispute Settlement Body adopted the report on November 1, 2002.

6. Canada's Challenge of Final Determination with Respect to Softwood Lumber

On March 21, 2002, Commerce announced its affirmative final CVD determination with respect to softwood lumber from Canada. On May 3, 2002, Canada requested WTO consultations with the United States, alleging that various aspects of the initiation of the CVD investigation and the final determination are inconsistent with the Subsidies Agreement and the GATT 1994.

Canada challenges several aspects of Commerce's determination. Among other things, Canada claims that Commerce's initiation of the investigation was not based on an objective assessment of the level of support for the petition because the Continued Dumping and Subsidy Offset Act (or "Byrd Amendment") by requiring that U.S. companies support the petition as a condition of receiving payments under the Byrd Amendment, makes an objective assessment impossible.

Canada also challenges Commerce's determination that provincial "stumpage" fees (the fees that the provincial governments charge for harvesting trees on public land) confer a subsidy because the provinces charge lower fees than private suppliers in northern U.S. states. Canada claims, among other things, that stumpage does not provide a "good" that can be countervailed under the terms of the Subsidies Agreement, that stumpage does not benefit a "specific" industry, that Commerce improperly assumed that the subsidy passed through arm's-length sales to downstream users of timber, and that prices charged by Canadian, rather than U.S., private suppliers are the proper benchmark for determining whether stumpage conveys a subsidy.

Canada also claims that Commerce failed to conduct its investigation in accordance with substantive and procedural requirements of the Subsidies Agreement for CVD investigations, arguing that Commerce refused to consider certain evidence, relied on information not made available to the parties, failed to issue timely decisions, and imposed unreasonable briefing schedules.

Canada filed its first written submission in the case on December 19, 2002, and the United States filed its first written submission on January 22, 2003. The first meeting of the panel is scheduled to be held on February 11-12, 2003. The second written submissions are due on March 6, 2003, and the second meeting of the panel is scheduled to be held on March 25-26, 2003.

7. Brazil Cotton

On September 27, 2002, the United States received from Brazil a request for consultations pursuant to Articles 4.1, 7.1 and 30 of the Agreement on Subsidies and Countervailing Measures, Article 19 of the Agreement on Agriculture, Article XXII of the General Agreement on Tariffs and Trade 1994, and Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes. The Brazilian letter requests consultations pertaining to "prohibited and actionable subsidies provided to U.S. producers, users and/or exporters of upland cotton, as well as legislation, regulations, statutory instruments and amendments thereto providing such subsidies (including export credits), grants, and any other assistance to the U.S. producers, users and exporters of upland cotton [footnote omitted]." Brazil claims that these alleged subsidies and measures are inconsistent with U.S. commitments and obligations under the Agreement on Subsidies and Countervailing Measures, the Agreement on Agriculture, and the General Agreement on Tariffs and Trade 1994. Consultations were held on December 3, 4 and 19 of 2002, and January 17, 2003.

C. NON-U.S. WTO DISPUTES WITH SYSTEMIC IMPORTANCE

Canada – Export Credits and Loan Guarantees for Regional Aircraft

In early January, 2001, Canada announced that it would respond in part to Brazil's refusal to withdraw certain export subsidies to the Brazilian regional aircraft manufacturer by offering financing for a deal involving the Canadian regional aircraft manufacturer and a U.S. airline. Brazil responded by requesting consultations and, ultimately, the formation of a WTO dispute settlement panel, challenging various Canadian programs "as such" and "as applied." It also challenged certain specific transactions under those programs. The United States participated in the dispute as a third party.

The panel issued its decision in January 2002. It rejected Brazil's challenges to the programs "as such" and refused to make findings on the programs "as applied." However, it found in favor of Brazil with respect to certain transactions, including the transaction involving the U.S. carrier.

Neither Canada nor Brazil appealed the Panel's report. Brazil then requested authorization to take countermeasures against Canada in the amount of US$ 3.36 billion. In December 2002, a WTO arbitrator issued a decision authorizing Brazil to take such measures in the amount of US$ 250 million. Canada had previously received authorization to take countermeasures against Brazil in the amount of US$1.4 billion. Brazil and Canada are presently engaged in discussions to resolve the matter.

CONCLUSION

In the coming year, USTR and Commerce will continue the vigorous enforcement of the rules and disciplines of the WTO Subsidies Agreement and take advantage of the opportunity provided by Doha Development Agenda rules negotiations to take strong, proactive steps to address the impact of distortive subsidies on American firms and their workers in both the United States and foreign markets. To accomplish this, the Administration, working together with Congress, will assertively put forward its affirmative agenda consistent with our negotiating objectives in order to achieve our goal of strengthening the international subsidy discipline regime and addressing the subsidy concerns of key sectors of the U.S. economy.

The Administration has now laid the groundwork in the context of the OECD steel initiative for addressing the long term structural problems afflicting the global steel industry. The unprecedented series of discussions among the world's major steel-producing countries culminated in a landmark decision to begin work on an agreement for reducing or eliminating trade-distorting subsidies in steel. The United States will take full advantage of this historic opportunity by actively leading the discussions and pushing for the strongest possible disciplines on government intervention in the steel sector.

As we move forward throughout the upcoming year, we will continue to work with the Congress as we pursue a proactive agenda to safeguard the interests of U.S. industries and workers facing unfairly subsidized foreign competition.

ATTACHMENT 1

WTO SUBSIDY NOTIFICATIONS REVIEWED IN 2002

WTO MEMBER	1998 New & Full Notifications	1999 Updating Notifications	2000 Updating Notifications	2001 Updating and New and Full Notifications
ANTIGUA				X
AUSTRALIA				X
BARBADOS				X
BELIZE				X
BOTSWANA				X
BURUNDI				X
CANADA			X	
CHILE				X
CHINESE TAIPEI				X
COLOMBIA				X
COSTA RICA				X
CROATIA				X
DOMINICA				X
DOMINICA REPUBLIC				X
EL SALVADOR				X
EU (incl. 15 member states)				X
FIJI				X
GHANA				X
GRENADA				X
GUATEMALA				X
HUNGARY	X			
INDIA				X
JAMAICA				X
JAPAN		X		X
JORDAN				X
KOREA				X
LATVIA				X
MALI				X
MAURITIUS				X
NAMIBIA				X

WTO MEMBER	1998 New & Full Notifications	1999 Updating Notifications	2000 Updating Notifications	2001 Updating and New and Full Notifications
NORWAY				X
PANAMA				X
PAPUA NEW GUINEA				X
PARAGUAY				X
ST. KITTS				X
ST. LUCIA				X
ST. VINCENT				X
SINGAPORE				X
SLOVENIA			X	X
SURINAME				X
TURKEY				X
UNITED STATES		X	X	X
URUGUAY				X
ZIMBABWE				X

ATTACHMENT 2

Extension of the Transition Period Pursuant to Article 27.4 of the Agreement on Subsidies and Countervailing Measures		
WTO MEMBER	**NAME OF PROGRAM**	**SUBSIDIES COMMITTEE ACTION****
ANTIGUA & BARBUDA	Fiscal Incentives Act*	5 year extension.
	Free Trade/Processing Zones*	5 year extension.
BOLIVIA (Annex VII Country)	Free Zone	Reservation of rights. No action taken.
	Temporary Admission Regime for Inward Processing	Reservation of rights. No action taken.
BARBADOS	Fiscal Incentive Program*	5 year extension.
	Export Allowance*	5 year extension.
	Research & Development Allowance*	5 year extension.
	International Business Incentives*	5 year extension.
	Societies with Restricted Liability*	5 year extension.
	Export Re-discount Facility	1 year extension.
	Export Credit Insurance Scheme	1 year extension.
	Export Finance Guarantee Scheme	1 year extension.
	Export Grant & Incentive Scheme	1 year extension.
BELIZE	Fiscal Incentives Program*	5 year extension.
	Export Processing Zone Act*	5 year extension.
	Commercial Free Zone Act*	5 year extension.
	Conditional Duty Exemption Facility*	5 year extension.
COSTA RICA	Duty Free Zone Regime*	5 year extension.
	Inward Processing Regime*	5 year extension.
COLUMBIA	Free Zone Regime	2 year extension.
	Special Import-Export System for Capital Goods & Spare Parts (SIEX)	2 year extension.
	Transport Compensation Mechanism	No decision taken.
DOMINICA	Fiscal Incentives Program*	5 year extension.
DOMINICAN REPUBLIC	Law No. 8-90, to “Promote the Establishment of Free Trade Zones*	5 year extension.
EL SALVADOR	Export Processing Zones & Marketing Act*	5 year extension.
	Export Reactivation Law	1 year extension.
FIJI	Short-Terms Export Profit Deduction	5 year extension
	Export Processing Factories/Zones Scheme	5 year extension
	The Income Tax Act (Film Making & Audio Visual Incentive Amendment Degree 2000)	5 year extension

WTO MEMBER	NAME OF PROGRAM	SUBSIDIES COMMITTEE ACTION**
GRENADA	Fiscal Incentives Act No. 41 of 1974*	5 year extension.
	Qualified Enterprise Act No. 18 of 1978*	5 year extension.
	Statutory Rules and Orders No. 37 of 1999*	5 year extension.
GUATEMALA	Special Customs Regimes*	5 year extension.
	Free Zones*	5 year extension.
	Industrial and Free Trade Zones (ZOLIC)*	5 year extension.
HONDURAS (ANNEX VII COUNTRY)	Free Trade Zone of Puerto Cortes (ZOLI)	Reservation of rights. No action taken.
	Export Processing Zones (ZIP)	Reservation of rights. No action taken.
	Temporary Import Regime (RIT)	Reservation of rights. No action taken.
JAMAICA	Export Industry Encouragement Act*	5 year extension.
	Jamaica Export Free Zone Act*	5 year extension.
	Foreign Sales Corporation Act*	5 year extension.
	Industrial Incentives (Factory Construction) Act*	5 year extension.
JORDAN	Income Tax Law No. 57 of 1985, as amended*	5 year extension.
KENYA (ANNEX VII COUNTRY)	Export Processing Zones	Reservation of rights. No action taken.
	Export Promotion Program Customs & Excise Regulation	Reservation of rights. No action taken.
	Manufacture Under Bond	Reservation of rights. No action taken.
MAURITIUS	Export Enterprise Scheme*	5 year extension.
	Pioneer Status Enterprise Scheme*	5 year extension.
	Export Promotion*	5 year extension.
	Freeport Scheme*	5 year extension.
PANAMA	Export Processing Zones*	5 year extension.
	Official Industry Register*	5 year extension.
	Tax Credit Certificates (CAT)	1 year extension.
PAPUA NEW GUINEA	Section 45 of the Income Tax Act*	5 year extension.

WTO MEMBER	NAME OF PROGRAM	SUBSIDIES COMMITTEE ACTION**
SRI LANKA (ANNEX VII COUNTRY)	Income Tax Concessions	Reservation of rights. No action taken.
	Tax Holidays & Profits Generated	Reservation of rights. No action taken.
	Concessionary Tax on Dividends	Reservation of rights. No action taken.
	Indirect Tax Concessions - Internal Tax Exemptions	Reservation of rights. No action taken.
	Export Development Investment Support Scheme	Reservation of rights. No action taken.
	Import Duty Exemption	Reservation of rights. No action taken.
	Exemption from Exchange Control	Reservation of rights. No action taken.
ST. KITTS & NEVIS	Fiscal Incentives Act*	5 year extension.
ST. LUCIA	Fiscal Incentives Act*	5 year extension.
	Micro & Small Scale Business Enterprise Act*	5 year extension.
	Free Zone Act*	5 year extension.
ST. VINCENT AND THE GRENADINES	Fiscal Incentives Act*	5 year extension.
SURINAME	Exemption on Social, Cultural, Educational Area	Request withdrawn
	Exemption to Stimulation National Production	Request withdrawn
	Exemption Based on International Regulation	Request withdrawn
THAILAND	Investment Promotion Incentives	1 year extension.
	Industrial Estate Authority of Thailand	1 year extension. 2 year required phase out.
	Export Market Diversification Program	No action taken.
URUGUAY	Automotive Industry Export Promotion Regime*	5 year extension.

* Program qualifies under special procedures adopted at the Fourth Ministerial Conference.
**All programs for which an extension was requested are permitted a two-year phase-out period after the extension period sanctioned by the Subsidies Committee. If no extension period was approved, Members must phase-out the program in two years.

ATTACHMENT 3

THE SUBSIDIES ENFORCEMENT LIBRARY

[http://ia.ita.doc.gov/esel/]

First Screen

ELECTRONIC SUBSIDIES ENFORCEMENT LIBRARY

< **WTO Agreement on Subsidies and Countervailing Measures**
< **Overview of the Subsidies Enforcement Office**
< **Subsidy Programs Investigated by DOC**
< **WTO Subsidies Notifications**

Reports to Congress

< **1998 Annual Report on Subsidies Enforcement - February 1998**
< **1999 Annual Report on Subsidies Enforcement - February 1999**
< **2000 Annual Report on Subsidies Enforcement - February 2000**
< **2001 Annual Report on Subsidies Enforcement - February 2001**
< **2002 Annual Report on Subsidies Enforcement - February 2002**
< **2003 Annual Report on Subsidies Enforcement - February 2003**

< **Review and Operation of the WTO Subsidies Agreement - June 1999**

Description of Choices

WTO Agreement on Subsidies and Countervailing Measures

This links the visitor to the World Trade Organization Agreement on Subsidies and Countervailing Measures as found in the Multilateral Agreement on Trade in Goods. Information in this Agreement includes the definition of a subsidy and provides general guidelines under which remedies may be put in place.

Overview of the Subsidies Enforcement Office

This links the visitor to the informational page found in Attachment 1 to this Report. As shown in Attachment 1, information contained on this page includes a general overview of the SEO as well as contact information.

Subsidy Programs Investigated by DOC

This links the visitor to information regarding subsidy programs which were analyzed by Import Administration staff during countervailing duty (CVD) proceedings. This section is newly redesigned and will more easily provide visitors access to the information which they are seeking. After clicking on the above choice, visitors will be linked to a page which has an alphabetical drop-down list of countries which were investigated during CVD proceedings. As of December 2002, this list comprised 52 countries. After selecting a country to review, visitors have the option of selecting subsidy programs within that country that are not specific to a certain industrial sector ("general") or programs that are used only by certain sectors ("industry").

Argentina					
Subsidy Type	**Program Codes**				
General	**1**	**2**	**3**	**4**	**5**
Industry	**1**	**2**	**3**	**4**	**5**

For example, if a visitor were interested in finding more information about subsidies to the steel sector in Argentina, he or she would click on the "Industry" link in the above table and then examine the information provided. Once a subsidy program of interest is found in this section, visitors are provided a description of the program and are able to easily view the cases in which the program was analyzed. Further information about the program in a specific case can be easily found by clicking on the hyperlinked cite to the Federal Register notice in which a complete description of the program and Commerce's analysis is provided.

The second sub-division of programs within this topic, as shown above, is based on the classification of the subsidy program by Commerce. There are five categorizations: (1) countervailable, (2) not countervailable, (3) terminated, (4) not used, and (5) found not to exist. These categories track the methodology used by Commerce and found in its decisions as published in the Federal Register. Descriptions for each of these terms are provided in the Subsidies Library. This level of detail allows a visitor to the library to easily find the exact type of information he or she is seeking.

Using the same example as described above, if a visitor were interested in discovering which subsidy programs Commerce had countervailed involving steel products exported from Argentina, he or she would select ***Argentina ± Industry ± Countervailable Programs*** and then review the information provided. If more detailed information about a particular subsidy program is required, a click of the mouse on the Federal Register cite next to the individual cases will take the visitor directly into the Federal Register notice where such information is readily available.

The following list shows the 52 U.S. trading partners which have had programs investigated in U.S. CVD proceedings. Information about each of these countries' investigated subsidy programs can be found in the Subsidies Enforcement database:

Argentina	**European Union**	**Korea**	**Singapore**
Australia	**France**	**Luxembourg**	**South Africa**
Austria	**Germany**	**Malaysia**	**Spain**
Bangladesh	**Greece**	**Mexico**	**Sri Lanka**
Belgium	**Hungary**	**Netherlands**	**Sweden**
Brazil	**India**	**New Zealand**	**Taiwan**
Canada	**Indonesia**	**Norway**	**Thailand**
Chile	**Iran**	**Pakistan**	**Trinidad and Tobago**
Colombia	**Ireland**	**Peru**	**Turkey**
Costa Rica	**Israel**	**Philippines**	**United Kingdom**
Denmark	**Italy**	**Poland**	**Uruguay**
Ecuador	**Japan**	**Portugal**	**Venezuela**
El Salvador	**Kenya**	**Saudi Arabia**	**Zimbabwe**

Descriptions of Choices (continued)

WTO Subsidies Notifications

This will link the visitor to all derestricted WTO subsidy notifications, by country. Beneath each country's name is the date the document was submitted to the WTO and the date it was posted to the WTO website. This listing provides each type of notification, i.e., ***new and full***, ***update*** or a ***supplement to an earlier filing***. (See discussion above in this Report.) Clicking on the name of the country next to the document of interest will take the visitor directly to that country's subsidy notification. If subsidies have been notified, a listing of those subsidies is provided, in addition to specific information concerning the subsidy program, such as the type of incentive provided, the duration and purpose of the program, and the governing law or provision of the incentive. Several of the larger countries have provided information on hundreds of subsidy practices. Although the Subsidies Agreement stipulates that the notification of a subsidy practice does not prejudge its legal status under the Agreement, these notifications do provide detailed information concerning a number of countries' subsidy measures. In the event that less than full information about the program is provided, the Subsidies Enforcement Office, working with other Agencies, seeks more detailed information.

Reports to Congress

< **1998 Annual Report on Subsidies Enforcement - February 1998**
< **1999 Annual Report on Subsidies Enforcement - February 1999**
< **2000 Annual Report on Subsidies Enforcement - February 2000**
< **2001 Annual Report on Subsidies Enforcement - February 2001**
< **2002 Annual Report on Subsidies Enforcement - February 2002**
< **2003 Annual Report on Subsidies Enforcement - February 2003**

Links are provided for the visitor to review the most recent SEO Annual Report to Congress as well as past Annual Reports.

Reports to Congress

< **Review and Operation of the WTO Subsidies Agreement - June 1999**

This links the visitor to the June 1999 Report to Congress that reviews the operation of the WTO Subsidies Agreement.

ATTACHMENT 4

TRADE REMEDY COMPLIANCE STAFF:

PRO-ACTIVELY ADDRESSING UNFAIR TRADE PROBLEMS

THE TRADE REMEDY COMPLIANCE STAFF

In recent years, Congress has called for more pro-active steps to address unfair practices hindering U.S. trade. To this end, it has provided both resources and a mandate for increased monitoring of other countries' trade policies and practices, as well as the strengthening of U.S. trade law enforcement. Import Administration (IA) has taken up that charge, in part through the creation of the Trade Remedy Compliance Staff (TRCS). The TRCS is a team of trade analysts working in tandem with new IA officers stationed overseas in such locations as China and Korea. Their mission is to support administration of the U.S. unfair trade laws, including by monitoring foreign policies and trade trends in order to better detect and address developing unfair trade problems.

THE TRCS ROLE AND SERVICE

IA's central role remains the enforcement of the U.S. antidumping (AD) and countervailing duty (CVD) laws. However, IA has built upon its law enforcement duties by instituting a variety of import monitoring and subsidies enforcement activities designed to help American industry deal more effectively with a broader range of unfair trade problems. The TRCS is the latest extension of this commitment to provide assistance to U.S. businesses which feel that their trade problems may stem from unfair practices or the improper application of foreign unfair trade laws. Focused initially on our major trading partners in east Asia, the TRCS has in place an ongoing monitoring program which tracks import trends as well as certain government policies, business conditions and company practices in the countries concerned. The goal is to help pinpoint and analyze problematic policies and trade trends so that governments have an opportunity to avert unfair trade frictions and prevent harm to U.S. interests. The placement of IA officers overseas gives the TRCS better access to various sources of information with which to more effectively identify and understand these potential unfair trade problems, as well as the ability to immediately address such problems, through discussion with government counterparts and technical assistance.

TRCS INITIATIVES UNDER WAY

For its key focus countries, TRCS personnel in Washington and abroad continually develop key information sources and databases to study imports into the United States and evaluate the status and evolution of foreign government policies and market developments that might contribute to unfair trade. On a wider front, TRCS keeps watch on all our trading partners' AD and CVD activity to identify potential difficulties for U.S. exporters and/or conflicts with WTO obligations or basic precepts of transparency and due process. One example of the TRCS's contributions thus far is its monitoring of China's WTO-related subsidies and unfair trade law obligations as part of the U.S. Government's broader efforts to verify Chinese compliance with WTO accession commitments.

TRCS Activities

Washington, D.C.

•For key countries, monitor data on imports into the United States, as well as foreign government policies and economic/business trends that may contribute to unfair trade problems.

•Monitor other countries' development and use of their AD, CVD and other trade remedy statutes.

•Provide information related to the enforcement of U.S. AD/CVD laws to foreign and domestic parties.

Overseas

•Support Washington-based case analysts in matters directly related to the administration of U.S. AD/CVD laws.

•Collect, assess, and confirm information about certain foreign market conditions, trade practices, and governmental policies that would facilitate administration of U.S. unfair trade laws or U.S. monitoring of unfair trade commitments.

•Report on developments in the use of foreign unfair trade laws, particularly as they affect U.S. interests.

•Actively assist countries to meet WTO obligations, through discussion and technical assistance.

Need further information?
Please contact:
Trade Remedy Compliance Staff
Tel: 202-482-3415/Fax: 202-482-6190

ATTACHMENT 5

SUBSIDIES ENFORCEMENT:
ASSISTING U.S. EXPORTERS TO COMPETE EFFECTIVELY

Subsidies Enforcement Office: The Department of Commerce's Import Administration is responsible for coordinating multilateral subsidies enforcement efforts. The primary mission is to assist the private sector by monitoring foreign subsidies and identifying government assistance programs that can be remedied under the Subsidies Agreement of the World Trade Organization, of which the United States is a member. To fulfill this mission, Import Administration has created the Subsidies Enforcement Office (SEO). As part of its monitoring efforts, the SEO has created a Subsidies Library, which is available to the public via the Internet (http://ia.ita.doc.gov/esel). The goal is to create an easily accessible one-stop shop that provides user-friendly information on foreign government subsidy practices.

Types of Subsidies: A subsidy can be almost anything a government does, if the following conditions are met: (1) a financial contribution is made by a government or public body and (2) a benefit is received by the company. Trade rules permit remedies in circumstances when subsidies are "specific" (*i.e.*, provided to a limited number of companies, such as all exporters) and have caused adverse trade effects. Subsidies can take a variety of forms. Following are some of the types of foreign subsidies that could place a U.S. exporter at a competitive disadvantage vis-a-vis a foreign competitor.

- ***Export financing*** at preferential rates.
- ***Grants or Tax exemptions*** for favored companies or industries.
- ***Loans that are conditioned on meeting local content requirements***, or are contingent upon the use of domestic goods over U.S. exports (commonly referred to as "import substitution subsidies").

As an illustration:
A U.S. exporter is bidding on a project in Country A and is competing against an exporter from Country B. The company from Country B offers a bid that is extremely low, possibly even below what one would assume to be the cost of production. The U.S. exporter may have knowledge that the reason the company from Country B is able to bid so low is that it is being assisted by its government with low cost loans and payment of various export related expenses. In such a situation, we would encourage the U.S. exporter to collect as much information as possible concerning the potential subsidies and then contact us with all of the relevant information. We would then check further into the types of subsidies being received and determine whether any action should be taken.

Types of Remedies: Remedies for violations of the Subsidies Agreement could involve requiring the foreign government to eliminate the subsidy program or its adverse effect, or, as a last resort, to authorize offsetting compensation.

Working Together to Assist U.S. Exporters: The SEO welcomes any information about foreign subsidy practices that may adversely affect U.S. companies' export efforts. The SEO can evaluate the subsidy in relation to U.S. and multilateral trade rules to determine what action may be possible to take to counteract such adverse effects. By working together to monitor foreign subsidies and enforce the WTO Subsidies Agreement, we can ensure that U.S. companies are competing in a fair international trading system.

***Questions and information can be referred to*:**
Carole Showers tel.: (202) 482-3217
fax : (202) 501-7952
e-mail: Carole_Showers@ita.doc.gov