

**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
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TABLE OF CONTENTS

Executive Summary	i
Introduction	1
Multilateral Initiatives	2
A. WTO Negotiations	2
B. Steel: Multilateral Efforts to Address Market-Distorting Practices	13
Monitoring and Enforcement	14
A. Advocacy Efforts	14
B. China.....	18
C. WTO Dispute Settlement and Other CVD Cases of Significance to Subsidies Disciplines	23
D. WTO Subsidies Committee.....	28
E. U.S. Monitoring of Subsidy-Related Commitments.....	31
Conclusion.....	33

EXECUTIVE SUMMARY

American workers and industries face significant competitive challenges from trade-distorting practices, including subsidies, which are employed by many foreign governments. The United States Government is committed to eliminating or neutralizing such practices when they adversely affect U.S. interests by pursuing its rights under the agreements of the World Trade Organization (WTO) and by ensuring that the United States' trading partners adhere to their obligations under those agreements. This report describes the efforts by the Office of the U.S. Trade Representative (USTR) and the U.S. Department of Commerce (Commerce), in close cooperation with other Executive Branch agencies, to monitor and challenge unfair foreign government subsidy practices worldwide in 2007. Section 281(f)(4) of the Uruguay Round Agreements Act mandates that USTR and Commerce submit a joint report to the Congress each year that describes the Administration's subsidy monitoring and enforcement activities throughout the previous year. This report is the thirteenth annual report submitted to the Congress.

The principal tool available to WTO Members to remedy harmful subsidy practices worldwide is the Agreement on Subsidies and Countervailing Measures (Subsidies Agreement, or Agreement), which establishes multilateral disciplines on subsidies. In the WTO, the Subsidies Committee serves as the primary forum for WTO Members' subsidy-related work and discussions. The United States actively participates in the Subsidies Committee to ensure the continued effectiveness of the Subsidies Agreement and seeks to deter or remedy harm caused to U.S. workers and industries from distortive subsidies through bilateral contacts, multilateral pressure and, where justified, WTO dispute settlement proceedings.

Another key and ongoing focus of U.S. subsidies enforcement activities is multilateral trade negotiations. In this regard, the United States continues to seek strengthened multilateral disciplines on subsidies through the WTO's Doha Development Agenda negotiations. These efforts should help expand and deepen the open, competitive and market-oriented trading environment that provides benefits to American consumers, producers and workers alike.

Doha Development Agenda

In November 2001, the latest round of global trade negotiations – known as the Doha Development Agenda (DDA) – was launched at the WTO's Fourth Ministerial Conference. In the Doha Ministerial Declaration, the United States secured a mandate to clarify and improve the disciplines under the Subsidies Agreement and the Agreement on Implementation of Article VI of the GATT 1994 (AD Agreement), and to address the trade-distorting practices that often give rise to the imposition of countervailing and antidumping duties. The ensuing six years of discussion and negotiation in the Rules Negotiating Group (Rules Group) recently culminated in the

release by the Chairman of the Rules Group, Ambassador Valles of Uruguay, of a draft negotiating text ("*Draft Consolidated Chair Texts of the AD and SCM Agreement*"). As discussed in more detail below, the release of this Chair's text marks the beginning of a new phase of more intense and focused consideration of the key elements of any final result in the Rules negotiations.

Since the beginning of this negotiation, the United States has sought to ensure that any final result of the negotiations is consistent with the Doha Rules mandate that the negotiations must preserve the basic concepts, principles and effectiveness of the two agreements and that Members' trade remedy laws are legitimate tools for addressing unfair trade practices that cause injury. In its first proposal, submitted in March of 2003, the United States outlined the basic U.S. objectives in seeking to strengthen the subsidy rules by calling for enhanced subsidy disciplines, identifying a broad array of issues with respect to the existing rules, and highlighting the need to develop new disciplines where none currently exist.

More recently, the United States has made important proposals to the Rules Group on the issue of prohibited subsidies. Noting that serious market and trade distortions can result from subsidies other than those currently prohibited by the Subsidies Agreement (*i.e.*, export subsidies and import-substitution subsidies), the proposals call for including several additional types of subsidies in an expanded prohibited category. These would include operating loss coverage, debt forgiveness, and loans and equity infusions to uncreditworthy and unequityworthy companies.

As noted above, in November 2007 Chairman Valles circulated a draft negotiating text, indicating that the intent behind the draft was to stimulate serious reflection on the "broad parameters of possible outcomes to the negotiations." Among the main issues and areas of subsidies rules addressed within the Chair's text are: definition of a subsidy, "dual pricing," serious prejudice, subsidy calculation methodologies, certain government lending practices, benefit pass-through, subsidy allocation, subsidy notification, export credits, and special and differential (S&D) provisions (annex VII of the Subsidies Agreement).

In its initial comments on the Chair's text, the United States noted, among other things, that the text would appear to result in little strengthening of the current general subsidy disciplines, despite the Doha mandate to clarify and improve the rules, and address trade-distorting practices. The United States further commented that the text regrettably did not reflect the U.S. proposal on prohibited subsidies or other proposals that would significantly strengthen the rules, such as the reinstatement of the "dark amber" provisions of Article 6.1 of the Subsidies Agreement. The United States urged the Chair and the other Members to rectify these deficiencies in subsequent versions of the text.

In addition to antidumping, countervailing and (general) subsidies-related issues, as part of the Doha mandate for Rules, Members have 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 United States views the negotiations on fisheries subsidies as a groundbreaking opportunity for the WTO to show that trade liberalization can benefit the environment and contribute to sustainable development as well as address traditional trade concerns. The United States continued to play a major role in advancing the discussion of fisheries subsidies reform in the Rules Group in 2007, working closely with a broad coalition of developed and developing countries, including Argentina, Australia, Chile, Ecuador, Iceland, New Zealand and Peru (collectively known as the “Friends of Fish”), as well as Brazil.

In March 2007, the United States submitted a paper providing draft textual language for a broad “top down” prohibition on subsidies to the harvesting of marine wild capture fisheries, with limited exceptions for subsidies that clearly do not promote overcapacity or overfishing. At the time of its submission, the proposal received considerable support, with many Members saying that some or all of it could be used as a basis for further negotiations. The proposal also was very well received by non-governmental organizations (NGOs) with an interest in environmental issues generally, as well as in these fishery negotiations in particular.

The Chair’s text on fisheries subsidies provides for fishery-specific disciplines in the form of a new annex to the Subsidies Agreement. The text reflects an ambitious proposal that would prohibit almost all of the most problematic forms of subsidies that contribute to overcapacity and overfishing in marine wild capture fisheries. Notably, the prohibition also includes a “catch all” provision that would prohibit additional subsidies if they confer benefits that affect fish stocks that are “unequivocally overfished.” The text has a narrow list of general exceptions available to all Members, and S&D provisions for developing countries. There are also provisions requiring fisheries management systems, notifications and surveillance, and peer review in the Food and Agriculture Organization (FAO) of the United Nations.

With the release of his November 30 text, the Chair has signaled that the Rules negotiations have now entered a “new phase involving further intensive discussions within the Group.” Additional plenary and plurilateral Rules meetings have been planned for early in 2008 to pursue a more in-depth discussion and negotiation of key issues included in the Chair’s text.

China

USTR and Commerce continued to aggressively confront a wide range of trade-distorting subsidies in China in 2007, through both multilateral and bilateral actions. Highlights include the decision by Commerce to apply the U.S. countervailing duty

(CVD) law to subsidized imports of Chinese goods for the first time, and an agreement with China to terminate a number of subsidies prohibited by WTO rules.

Commerce's decision to apply the U.S. anti-subsidy law to imports from China represents the first time that the U.S. countervailing duty law was applied to imports from a non-market economy. The decision alters a 23-year old policy of not applying the CVD law to non-market economy countries, and reflects the conclusion that reforms to China's economy in recent years had removed the obstacles to applying the CVD law that were present in the "Soviet-era economies" at issue when Commerce first declined to apply the CVD law to non-market economies in the 1980s. Applying the U.S. CVD law to potentially injurious subsidized imports from China demonstrates the Administration's commitment to leveling the playing field for American companies, workers and farmers.

The decision to apply the U.S. CVD law to China stemmed from a petition filed in October 2006 requesting the initiation of a CVD investigation regarding allegedly injurious subsidized imports of coated free sheet paper from China. The petition requested a change to Commerce's longstanding policy of not applying the U.S. CVD law to China or any other country considered a "non-market economy" for antidumping purposes. In its final determination in October 2007, Commerce found that China's paper industry benefitted from a wide range of countervailable subsidies, including some that are prohibited under WTO rules.¹ During 2007, several other U.S. industries concerned about subsidized Chinese imports also filed CVD petitions. As of the end of 2007, Commerce had initiated CVD investigations of allegedly subsidized Chinese imports of circular and rectangular steel pipe, laminated woven sacks, off-the-road tires, flexible magnets, thermal paper and sodium nitrite.

The subsidies Commerce investigated in the coated free sheet paper case, and those alleged and currently being examined in the ongoing proceedings listed above, include preferential policy loans, income tax and VAT exemptions and reductions, the provision of goods and services on non-commercial terms, and a variety of provincial and local government subsidies. Given some of the unique features of China's economy, a number of the subsidies investigated in these cases present novel and complex issues, from both a legal and methodological perspective. Commerce will continue to devote all the necessary resources to these proceedings.

During 2007, the Administration also demonstrated its strong commitment to challenge China's trade-distorting subsidies, including at the WTO, when serious dialogue failed to yield the necessary results. Through a series of high-level bilateral meetings in Beijing beginning in 2006, the United States made clear that China needed

¹ Commerce did not issue a final countervailing duty order for the coated free sheet paper case, because the U.S. International Trade Commission determined on November 20, 2007 that the U.S. industry was not injured by unfairly subsidized Chinese imports.

to withdraw both the prohibited subsidies that it had notified to the WTO Subsidies Committee and several additional apparently prohibited subsidies that it had not notified. The subsidies at issue benefited a wide range of industries in China and included both export subsidies, which make it more difficult for U.S. manufacturers to compete against Chinese manufactured goods in the U.S. market and third-country markets, and import substitution subsidies, which make it more difficult for U.S. manufacturers to sell their products in China.

When it became clear that continued bilateral dialogue would not resolve this matter, the United States, together with Mexico, initiated WTO dispute settlement proceedings against China. In November 2007, a settlement was reached in which China agreed to eliminate all of the subsidies at issue and not to reinstate them. Under the Memorandum of Understanding (MOU) signed by China and the United States, China committed to complete a series of steps by January 1, 2008 to ensure that the WTO-prohibited subsidies cited in the U.S. complaint have been permanently eliminated, and that they will not be re-introduced in the future. U.S. companies and workers will benefit from the removal of China's trade-distorting subsidies under the terms of the settlement much sooner than would have been possible if the United States had litigated this case to its conclusion. At the same time, if for any reason China does not meet its MOU commitments, the United States has the right to re-start WTO proceedings. This outcome demonstrates that serious dialogue and resolute enforcement can deliver real results, representing a victory for U.S. manufacturers and workers.

In 2008, the United States will continue to press China to comply fully with its obligations to eliminate all subsidies prohibited by WTO rules and to provide a full accounting of the range of subsidies maintained by all levels of government, as required by the Agreement.

Steel

The United States was very active this past year in multilateral, regional, and bilateral efforts to stress the need for market-driven rationalization of the world's excess, inefficient steelmaking capacity. Specifically, throughout 2007, the United States continued to play a key role in international efforts to address the structural issues which plague the global steel industry, particularly with respect to the frequency and magnitude of market-distorting government intervention in this market. Consistent with the President's 2001 Initiative on Steel, the primary goal of these efforts is to seek lasting solutions to the long-term problems in this industry, including oversupply, unfair trade competition and trade remedy responses. The North American Steel Trade Committee (NASTC) and the OECD Steel Committee continue to be valuable forums for exploring ways to promote the understanding of the industry's structural problems and approaches by which they can be addressed. In addition, this past year, the United States continued to engage the Chinese government in the Joint Commission on

Commerce and Trade (JCCT) U.S. – China Steel Dialogue on a variety of issues, including the problems that subsidies and other types of government intervention in the steel sector can cause in world steel markets.

Conclusion

The United States will continue to strengthen its efforts to ensure that American consumers, workers and companies benefit from a competitive, market-oriented global economy that is free of distortions brought on by unfair trade practices, such as subsidies. Specifically, the U.S. Government's subsidies enforcement program is committed to assisting American workers and companies that are threatened or harmed by distortive subsidy practices, whether domestically or in foreign markets, and it will strengthen that commitment by focusing its resources on identifying and challenging a wide range of unfair foreign government practices that adversely affect the interests of the United States. We will endeavor to resolve these issues through advocacy, negotiation or bilateral or multilateral contacts. However, the United States will not refrain from initiating WTO dispute settlement proceedings if its interests cannot be adequately addressed through advocacy and negotiation. In doing so, we will help ensure that U.S. consumers enjoy the full range of choice, quality and affordable prices that can only be obtained through engagement in a dynamic and competitive global economy.

INTRODUCTION

The Subsidies Agreement establishes multilateral disciplines on subsidies and provides mechanisms for challenging government programs that contravene these disciplines. 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. In addition, the Subsidies Agreement sets forth rules and procedures to govern the application of countervailing duty (CVD) measures by WTO Members with respect to injurious, subsidized imports.

The Subsidies Agreement nominally divides subsidy practices into three classes: prohibited (red light) subsidies; permitted yet actionable (yellow light) subsidies; and permitted non-actionable (green light) subsidies.² Export subsidies and import substitution subsidies are prohibited. All other subsidies are permitted, but are 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. With the expiration of the Agreement's provisions on green light subsidies, at present, the only non-actionable subsidies are those that are not specific, as defined above.

² 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 be treated as non-actionable subsidies. In addition, Article 6.1 of the Agreement provided that certain other subsidies (*e.g.*, subsidies to cover a firm's operating losses), referred to as dark amber subsidies, could be presumed to cause serious prejudice. 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 earlier Annual Subsidies Reports, these provisions expired on January 1, 2000, because a consensus could not be reached among WTO Members on whether to extend these provisions, or on the terms by which these provisions might be extended beyond their five-year period of provisional application.

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 WTO, including its Subsidies Committee, and chair the interagency process on matters of trade policy. The role of Commerce, through the International Trade Administration's Import Administration (IA), is to enforce the CVD law, monitor the subsidy practices of other countries, and provide the technical expertise needed to analyze and understand the impact of foreign subsidies on U.S. commerce. IA will also provide assistance and advice to interested U.S. parties concerning the remedies available under the Subsidies Agreement and the procedures relating to these remedies and, where warranted, recommend action to USTR.

Within IA, subsidy monitoring and enforcement activities are carried out by the Subsidies Enforcement Office (SEO). These activities are supported and complemented by the Trade Remedy Compliance Staff (TRCS), also located in IA. (See Attachments 1 and 2, which contain full descriptions of the SEO and TRCS.) IA continues to build upon and improve coordination of these different efforts to address pro-actively foreign unfair trade practices. 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, Agriculture and Treasury, and the Council of Economic Advisors -- concerning the full range of issues pertaining to the obligations of the United States' trading partners under the Subsidies Agreement.

The enactment of the Uruguay Round Agreements Act (URAA) in 1994 provided USTR and Commerce additional scope and focus 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 United States' monitoring and enforcement activities throughout the previous year. This report constitutes the thirteenth annual report to be transmitted to the Congress pursuant to this provision.

MULTILATERAL INITIATIVES

A. WTO NEGOTIATIONS

In November 2001, the latest round of global trade negotiations – known as the Doha Development Agenda (DDA) – was launched at the WTO's Fourth Ministerial Conference. In the Doha Ministerial declaration, the United States secured a mandate to clarify and improve the disciplines under the Subsidies Agreement and to address the trade-distorting practices that often give rise to the imposition of countervailing and

antidumping duties. Critically, the negotiating mandate of the Rules Negotiating Group (Rules Group) recognizes that the negotiations must preserve the basic concepts, principles and effectiveness of the Subsidies and AD Agreements and that Members' trade remedy laws are legitimate tools for addressing unfair trade practices that cause injury. Under this mandate, the United States has continued to pursue 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. However, other permitted subsidies can 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 trade remedies in a constructive manner. Moreover, it provides an avenue to take up the negotiating objectives that Congress had previously laid out in the Trade Act of 2002 and other subsidy concerns that affect key sectors of the U.S. economy. Consistent with the Doha mandate and the objectives of Congress, in 2007 the United States tabled draft text on an ambitious proposal in the WTO Rules Group to significantly strengthen the disciplines on subsidies by expanding the list of prohibited subsidies within the Subsidies Agreement (see further discussion of this proposal, below).

Another important component of the DDA is the work on disciplines specifically covering fisheries subsidies, which is included as part of the Rules negotiations. The United States has believed for some time that the depleted state of the world's fisheries stock is a major economic and environmental concern, and that subsidies that contribute to overcapacity and overfishing, or that have other trade-distorting effects, are a significant part of the problem. The inclusion of fisheries 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.

1. Progress to Date

a. General

The Rules Group has based its work primarily on the written submissions from Members, with the work organized into the following categories: (1) antidumping (often including similar issues relating to countervailing duty remedies); (2) subsidies, including fisheries subsidies; and (3) regional trade agreements. In 2007, under the chairmanship of Ambassador Guillermo Valles Galmes of Uruguay, the Group continued to intensify its work through a series of meetings throughout the year. As in earlier years, during this time the Rules Group met only infrequently in "formal" sessions, preferring "informal" and "plurilateral" sessions (comprised of smaller

groupings of Members who have shown the most interest in a particular negotiating topic) that facilitate more detailed technical discussions.

As discussed in further detail below, on November 30, 2007, Chairman Valles circulated a *Draft Consolidated Chair Texts of the AD and SCM Agreement* (“Chair’s text”).³ With the release of this text, the Chair has signaled that the Rules negotiations have now entered a “new phase involving further intensive discussions within the Group.” Additional plenary and plurilateral Rules meetings have been planned for early in 2008, to pursue a more in-depth discussion and negotiation of key issues included, and not included, in the Chair’s text.

b. Subsidies-Specific Submissions

As part of its active involvement in the Rules negotiations, the United States has submitted several subsidies-specific papers and proposals, starting with a U.S. submission in December 2002 on special and differential treatment for developing countries.⁴ In March 2003, the United States submitted its second subsidies-specific paper on the general need for improved disciplines.⁵ In this paper, the United States identified a broad array of subsidy issues with respect to the existing rules, and suggested areas for new disciplines where none currently exist. The U.S. position on subsidies has been firmly grounded in the negotiating objectives of the Trade Act of 2002. As noted above, the development of enhanced disciplines on trade-distorting practices, including subsidies, is particularly important because these practices are often the root cause of trade friction.⁶

In the years 2004 through 2007, the United States made seven additional written submissions, the first five of which specifically focused on the further development of subsidy calculation methodologies. While the Uruguay Round negotiations were successful in defining broad methodological concepts in the Subsidies Agreement regarding the measurement of various types of subsidies, the United States believes that greater detail is needed in certain areas to clarify the precise nature of Members’

³ See, TN/RL/W/213. (This document and other WTO public documents are available on the WTO website at <http://docsonline.wto.org>.)

⁴ See, TN/RL/W/33.

⁵ See, TN/RL/W/78.

⁶ Specifically, the U.S. March 2003 paper covered ten general topics: (1) expansion of the prohibited category of subsidies; (2) the “serious prejudice” provisions of the Subsidies Agreement; (3) indirect subsidies; (4) natural resource and energy pricing; (5) the provision of equity capital; (6) taxation; (7) royalty-based financing; (8) codification of analytical and calculation methodologies; (9) procedural issues; and (10) subsidy notifications.

obligations under the Subsidies Agreement and to establish a firmer basis for strengthened rules (e.g., quantitative limitations on subsidy benefit amounts). Therefore, the U.S. submissions generally addressed the following three issues of subsidy allocation: (1) when to allocate a subsidy over time; (2) how to allocate a subsidy over time; and (3) when allocating a subsidy over time, how to determine the length of time over which the allocation should occur. In its last paper to date on this topic, the United States submitted draft text for possible rules on subsidies allocation.⁷

The U.S. proposals on subsidy allocation have been the focus of formal and informal as well as plurilateral discussion and have been well received by many within the Rules Group. Many Members with interest in the issue have recognized that the U.S. papers on these topics raise the next set of questions that must be answered to continue the historical development of a general set of subsidy benefit calculation rules. Such rules are commonly viewed as critical to strengthening and increasing the predictability of the subsidy disciplines of the Subsidies Agreement.⁸

In addition to the papers on subsidy allocation, the United States made two submissions to the Rules Group in 2006-07 on the issue of prohibited subsidies. In a narrative that noted that serious market and trade distortions can result from subsidies other than those currently prohibited by the Subsidies Agreement (*i.e.*, export subsidies and import-substitution subsidies), the first paper⁹ urged Members to consider expanding the current prohibition to encompass other subsidies that most typically and directly impede industry restructuring and rationalization, and which often result in inefficient excess capacity. The second submission on prohibited subsidies¹⁰ followed up with proposed draft textual changes to the Subsidies Agreement. In this second submission, the United States identified the following types of subsidies as meriting inclusion in an expanded prohibited category:

- (a) the direct transfer of funds to cover operating losses sustained by an enterprise or industry;
- (b) forgiveness of debt, *i.e.*, forgiveness of government-held loans or other instruments of indebtedness, and grants to cover repayment of government-held loans or other instruments of indebtedness;

⁷ See, TN/RL/Gen/130.

⁸ Consistent with the broad support of other key Members on this issue, the United States' proposed text on subsidy allocation was reflected in Article 14.3 of the Chair's text.

⁹ See, TN/RL/Gen/94.

¹⁰ See, TN/RL/Gen/146.

- (c) loans and other instruments of indebtedness provided directly to enterprises that are uncreditworthy;
- (d) provision of equity capital where the investment decision is inconsistent with the usual investment practice (including for the provision of risk capital) of private investors in the territory of that Member; and
- (e) other financing (*i.e.*, "royalty-based" or "sales-contingent" financing or other similar financing) to an enterprise or project that otherwise would be unlikely to receive such financing from commercial sources.

In addition to proposing the expansion of the prohibited category, these two papers also put forth a progressive new proposal to address increasing concerns with foreign state-owned and state-controlled enterprises. The United States questions the justification for any government investment in the private sector in countries with well-developed capital markets. Government investment decisions that run counter to the private sector's assessment that a company is not likely to generate a market return should be made in a transparent fashion, closely scrutinized and, as appropriate, curtailed. Accordingly, the United States, pursuant to its 2007 submission, proposes that all Members notify the WTO Subsidies Committee of the following information regarding a government-owned company:

- (a) with respect to the provision of equity capital by any government or public body: the date and terms of the transaction; and an explanation of the consistency of the investment with the usual practice of private investors in the territory of that Member;
- (b) with respect to any government majority-owned, as well as government-controlled enterprises: the percentage of direct and indirect ownership that the government or any public body holds in the enterprise and the terms and conditions of any financial contribution by any government or public body to the government majority-owned or controlled enterprise, excluding non-specific instances in which government revenue that was otherwise due was foregone or not collected.

The potential importance of these proposals is considerable. They are the most far-reaching, discipline-enhancing proposals tabled to date in the Rules subsidies negotiations, reinforcing the United States' leadership in pursuing strong subsidies disciplines under the WTO. The proposed strengthened disciplines would greatly enhance the United States' ability to address, and potentially deter, subsidy-related unfair trade practices confronting U.S. industries.

During 2007, in addition to the prohibited subsidies proposal by the United States, much of the Rules Group's subsidies-related discussion focused on two items in the European Union's proposal on "Subsidies" (TN/RL/Gen/135). The first item is a proposed prohibition on "the provision, by virtue of government action, of goods to domestic production on terms and conditions more favorable than those generally available for such goods when destined for export." With this provision, the EU appears to be seeking to address what it and other WTO Members view as the subsidy or subsidy-like effect of natural resource pricing of certain countries.

The second item in the EU's proposal, "below cost financing," pertains to situations where financing is available to economic operators at rates which do not cover the full cost of such financing. The European Union has noted that such practices may be particularly difficult to address under current Subsidy Agreement rules, and that one solution would be the introduction of specific language to the effect that loans granted at below-cost rates would be subject to disciplines if such practices are found to be generalized and systematic, resulting from widespread government interference.

Several other Members also have made important proposals in the Rules Group concerning subsidy-related issues, some of which were discussed further in 2007. The Subsidies Enforcement Annual Reports to Congress of prior years have provided summaries of these key proposals.¹¹

c. Fisheries Subsidies

As part of the Doha mandate, Members have 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 United States views the negotiations on fishery subsidies as a groundbreaking opportunity for the WTO to show that trade liberalization can benefit the environment and contribute to sustainable development as well as address traditional trade concerns. The United States continued to play a major role in advancing the discussion of fisheries subsidies reform in the Rules Group in 2007, working closely with a broad coalition of developed and developing countries, including Argentina, Australia, Chile, Ecuador, Iceland, New Zealand and Peru (collectively known as the "Friends of Fish"), as well as Brazil.

Although a broad consensus has emerged in favor of stronger disciplines, including a prohibition of the most harmful subsidies (*i.e.*, those that contribute to overfishing and overcapacity), throughout 2007 there remained disagreement over the structure of such disciplines, as well as their extent and coverage. The United States and Friends of Fish have generally advocated a framework encompassing a broad-

¹¹ Australia made two submissions early in 2007 following up on earlier proposals (See, TN/RL/GEN/80/Rev.1 and TN/RL/GEN/115/Rev.1). Late in 2007, India made a submission to the Rules Group that was scheduled to be discussed in January 2008. See, TN/RL/GEN/153.

based prohibition (*i.e.*, a “top down” approach), with appropriate, well-defined exceptions. Specifically, the United States has preferred a prohibition focused on subsidies that contribute to overcapacity and overfishing and consideration of carefully targeted exceptions to allow appropriate flexibility. In contrast, some other Members, such as Japan, Korea and the European Union, have advocated a “bottom up” approach allowing for a large number of permitted subsidies and a small number of prohibited subsidies (*i.e.*, those that cause demonstrable adverse resource and trade effects).

In March 2007, the United States submitted a paper, entitled “Fisheries Subsidies: Proposed New Disciplines,” providing draft textual language for a broad prohibition on subsidies to the harvesting of marine wild capture fisheries.¹² At the time of its submission, the proposal received considerable support, with many Members saying that some or all of it could be used as a basis for further negotiations. Several of the ideas within the U.S. proposal were also subsequently reflected in the first version of the Chair’s text. The disciplines in the U.S. proposal are rooted within the existing structure and concepts of the Subsidies Agreement, including the definition of “subsidy” and “specificity.” The proposal does not cover aquaculture, although subsidies relating to associated wild capture activities would be prohibited. Subsidies for on-vessel fish processing and transportation from one vessel to another vessel or to shore also would be covered.

The U.S. proposal lists several subsidy programs that are not subject to the prohibition because they do not normally promote overcapacity and overfishing. These include: governmental assistance for vessel decommissioning; financing of user-specific quota allocation management schemes; fisheries management research; measures to enhance marine resources (such as fisheries stock and marine environment enhancement programs), construction and maintenance of infrastructure for fishing communities (such as housing, roadways and sanitary waste – but not fishing ports); certain social programs to assist fishermen; replacement of fishing capacity following natural disasters; and improvement of vessel and crew safety. Payments received by a coastal state from a distant water government for fisheries access are excepted from the prohibition; however, the further transfer of the rights from the distant water government to its fleet are prohibited unless the fleet provides compensation in the amount of the cost the fleet would otherwise have to pay, the terms and conditions are made public and the access arrangement provides for a science-based assessment, monitoring and compliance mechanism for fisheries management.

Furthermore, while no specific text was offered on this particular issue, the U.S. proposal contemplates an additional exception for small programs, which by virtue of the small benefits conferred, do not contribute to overcapacity and overfishing.

¹² See, TN/RL/GEN/145.

Importantly, to avoid loopholes and to retain Members' rights regarding actionable subsidies under the existing Subsidies Agreement, exceptions to the prohibition would remain subject to WTO legal challenge if they cause serious prejudice to other Members. The proposal also provides additional serious prejudice criteria to adapt the rules to the fisheries context.

The Subsidies Enforcement Annual Reports to Congress of prior years have provided detailed overviews of the key proposals from other Members, and which for the sake of brevity will not be repeated here. Throughout 2007, several of these proposals by various Members were further revised and discussed by the Rules Group at length. A key part of this discussion has been an increased focus on the issue of special and differential (S&D) provisions for fisheries disciplines. Many of the framework proposals from developed and developing countries alike have attempted to deal with the difficult issues of small scale fishing, artisanal fishing, *de minimis* rules and access fees, fisheries management and stock assessment, and how these may or may not be part of any S&D provisions. Most notable and promising in the area of fisheries S&D were proposals by Argentina and Brazil, which were later combined into a single revised proposal.¹³

The issues that arise in the area of fisheries S&D, however, are conceptually and technically quite complex. Some concepts, such as "small scale" or "artisanal," for example, do not have a single, commonly accepted definition, and other areas involving fisheries management and stock assessments can involve areas of expertise in fishery resources that are traditionally outside the competence of the WTO. Accordingly, broad agreement on these issues within the Rules Group has been difficult to achieve. The United States and other Friends of Fish nevertheless remain committed to working with all Members to address the practical problems that developing countries may face in implementing stronger disciplines on fisheries subsidies.

d. *Chair's Text on General and Fisheries Subsidies Disciplines*

At the Hong Kong Ministerial Conference in December 2005, Ministers directed the Rules Chairman to prepare consolidated texts of the AD and Subsidies Agreements early enough to ensure a timely outcome within the context of the then-presumed 2006 end date for the Doha Agenda negotiations and taking account of progress in other areas of the negotiations. Although the release of these consolidated texts was delayed by subsequent developments in other negotiating areas of the Doha Round, on November 30, 2007, Chairman Valles circulated a *Draft Consolidated Chair Texts of the AD and SCM Agreement*. In a cover note to this text, the Chairman indicated that the intent behind the draft was to stimulate serious reflection on the "broad parameters of possible outcomes to the negotiations" and that he has tried to facilitate the negotiation

¹³ See, TN/RL/Gen/151/Rev.1.

of a balanced outcome. He further noted that the Chair's text does not reflect all proposals by all Members and that, pending further guidance from Members, such additional proposals might be reflected in later drafts.

The following is a brief overview of the main concepts and proposed changes reflected in the Chair's text pertaining to the general subsidies (*i.e.*, separate from Annex VIII of the Chair's text which is exclusive to fisheries subsidies) proposals, with references to the specific relevant provisions of the Subsidies Agreement.

- Definition of a Subsidy (Article 1, footnote 2): Clarifies that the subsidy "benefit" is to be determined in reference to what would be otherwise available to the subsidy recipient in the market, including, where applicable, use of Article 14 countervailing duty subsidy benefit quantification guidelines.
- "Dual Pricing" (Article 2.1(c) and Article 14(d)): Addresses situations in which a government provides goods at regulated prices and allows for a finding of "specificity" when a government excludes certain companies from access to the good at the regulated price. When calculating the subsidy benefit, the newly-added provision of Article 14(d) allows reference to export prices or a market-determined price outside the country as a benchmark if no undistorted domestic price is available.
- Fishery Subsidies Prohibition (Article 3): Includes a newly-added category for prohibited fisheries subsidies (Article 3.1(c)). Footnote six clarifies that, in accordance with certain dispute settlement panel reports, the description of certain export subsidies in Annex I shall not be used to establish by negative implication that a measure does not constitute an export subsidy.
- Fishery Subsidy Remedies: Footnotes 10 and 11 identify certain "countermeasures" (*e.g.*, suspension of access to port facilities) that can be taken in instances of violation of new fisheries subsidies rules.
- Serious Prejudice (Article 6.4): Clarifies how displacement or impedance of imports shall be evaluated (*i.e.*, using the same existing standard as displacement or impedance of exports into third country markets).
- Subsidy Calculation Methodology (Article 14): In conjunction with newly-added footnote 2 to Article 1, confirms that subsidy benefit calculations should be in accordance with the "benefit to the-recipient" approach rather than the "cost to government" approach.
- Loan and Loan Guarantee Subsidy Calculation (Article 14(b) and (c) and footnote 46): Establishes a rebuttable presumption that a benefit has been conferred

when a loan or loan guarantee is provided by certain banks incurring long-term operating losses costs on the provision of such financing as a whole.

- Pass-through Analysis (Article 14.2): Requires that in order to attribute a subsidy to an input to a downstream product, it must be demonstrated that the input was obtained on terms more favorable than those commercially available in the market or, where that market is distorted, in relation to other sources such as world market prices.
- Treatment of Subsidy Benefits Over Time (Article 14.3): Incorporates the U.S. subsidy allocation proposal, which is consistent with U.S. CVD practice.
- Subsidy Notification (Articles 25 & 26): Codifies a previously-agreed understanding that Members are required to provide a “new and full” subsidy notification every other year, with no intervening “updating” notifications.
- Export Credits (Annex I/item k): Establishes the benchmark for government export credits as the rate available to the recipient in international capital markets rather than the cost of funds to the providing government. Requires that any revision to the Organization for Economic Cooperation and Development (OECD) agreement on export credits (incorporated by reference into the WTO Subsidies Agreement) be “examined” by the WTO Subsidies Committee before revised rules become binding on the WTO membership.
- Special and Differential (Annex VII/footnote 76): Codifies language agreed to by Ministers at Doha Fourth Ministerial Conference; modifies threshold for “Annex VII(b)” developing country “graduation”.

Notably absent from this version of the Chair’s text were any proposed changes to the CVD provisions corresponding to proposals that were incorporated into the Chair’s text for the AD Agreement on issues of common relevance between the two agreements. In the cover note to his draft text, Chairman Valles noted that, “since the beginning of these negotiations, there has been a broad acceptance that changes to the antidumping rules should, where relevant and appropriate, also be made to the rules regarding countervailing measures.” He further explained, however, that he did not reflect any such changes in his text “because such a transposition will require further technical discussion.”

At the meeting of the Rules Group the week of December 12, 2007, the United States presented an initial summary response to the Chair’s text, in which it noted, among other things, that the Chair’s text results in little strengthening of the current general subsidy disciplines -- contrary to the Doha mandate to clarify and improve the rules and address trade-distorting practices. Specifically, the text regrettably does not

reflect the U.S. proposal on prohibited subsidies or other proposals that would significantly strengthen the rules, such as the reinstatement of the Article 6.1 “dark amber” provisions. The United States exhorted the Chair and the other Members to rectify these deficiencies in subsequent versions of the text as part of an ultimate balanced package on Rules overall. The United States also urged that the process of determining which provisions of the AD draft text should be included in the Subsidies Agreement be started as soon as possible, given that each potential change would need to be scrutinized within the context of the object and purpose of the Subsidies Agreement in order to assess the validity and appropriateness of each proposed change.

On fisheries subsidies, the Chair’s text provides for fishery-specific disciplines in the form of a new annex to the Subsidies Agreement. The text reflects an ambitious proposal that would prohibit almost all of the most problematic forms of subsidies that contribute to overcapacity and overfishing in marine wild capture fisheries. Although the text adopts a “bottom up” approach (*i.e.*, lists specific prohibited subsidies) rather than a “top down” broad prohibition, the prohibited list is quite comprehensive, including all subsidies related to capital costs (vessel acquisition, construction, etc.), operational costs (including fuel, bait and ice), fisheries-related infrastructure, in- or near-shore processing, and subsidies arising from the transfer of access rights to fish in another WTO Member’s fisheries jurisdiction, unless conditions related to fisheries management and transparency are met. The prohibition also includes a “catch all” provision that would prohibit additional subsidies if they confer benefits that affect fish stocks that are “unequivocally overfished.” The text has a narrow list of general exceptions available to all Members, and S&D provisions for developing countries. There are also provisions requiring fisheries management systems, notifications and surveillance, and peer review in the Food and Agriculture Organization (FAO) of the United Nations.

In discussing the Chair’s text for the first time at the December 2007 Rules meeting, Members stated their support for using the Chairman’s fisheries subsidies text as a basis for further negotiations. While expressing some disappointment that the text does not use the “top down” approach, the United States and other Friends of Fish praised its ambition, noting that it would be a landmark for the WTO in delivering a potential “win-win-win” for the environment, trade and sustainable development. The opponents of strong fisheries disciplines – the European Communities, Japan, Korea and Chinese Taipei – primarily focused on the scope of the items listed in the prohibition, specifically objecting to the prohibition of subsidies relating to operating costs (notably fuel), infrastructure (ports and handling facilities), and fish processing.

Most Friends of Fish and several other countries generally supported the exceptions to the prohibition that are included in the text, highlighting that the S&D provisions permitted subsidies by a developing country only for fishing within its Exclusive Economic Zone (EEZ), and required satisfaction of detailed “sustainability”

conditions associated with stock and capacity assessment and management. The United States and others also strongly endorsed the fact that all fisheries subsidies (even those subject to exceptions from the prohibition) would remain subject to existing subsidy disciplines (*i.e.*, would remain “actionable”), including through countervailing duty proceedings.

Several developing countries argued that the S&D provisions were too limited and that the conditions to qualify were too detailed and prescriptive, particularly with respect to fisheries management and FAO peer review requirements. Specifically, certain developing countries expressed the view that operating cost subsidies and subsidized activities for fishing outside a developing country’s EEZ should be permitted. Some developing countries were also critical of the treatment of artisanal and small-scale fisheries, particularly the fisheries management requirements, which they considered to be too burdensome. Notably, however, there was broad agreement among developed and developing countries alike that the provisions on access arrangements were appropriate.

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

In 2007, the United States continued to address concerns related to the rapidly changing trade situation in the global steel sector, through its work at the OECD, the North American Steel Trade Committee (NASTC) and the U.S. – China Steel Dialogue under the Joint Commission for Commerce and Trade (JCCT).

The United States worked closely with the OECD Secretariat as well as the governments of other steel-producing economies to take up policy issues affecting the global steel industry. The OECD covered a broad range of issues in 2007, including capacity expansion, government subsidies in the steel sector, restructuring and consolidation of the global steel industry, environmental issues, R&D and raw materials. The United States was a key supporter of and participant in the Secretariat’s survey of subsidies to the steel sector and was a strong advocate for broad participation in this ongoing exercise. The United States also backed efforts by the OECD Secretariat to reach out to developing steelmaking economies, including the Secretariat’s organization of a major steel conference focused on consolidation in the steel industry held in May 2007 in Istanbul, Turkey, and jointly hosted by the OECD, the Government of Turkey and the International Iron and Steel Institute, a global steel industry association.

The governments and steel industries of North America continued their efforts to examine and pursue common policy approaches to promote the competitiveness of North American steel producers through the NASTC. An initiative under the North American Security and Prosperity Partnership (SPP), the NASTC developed a North American Steel Strategy in 2006 that includes cooperation on issues of importance to

steel in multilateral fora (e.g., the OECD Steel Committee and the WTO Rules Negotiations). Under the NASTC, the three North American governments and steel industries have been tracking developments in certain steel-producing countries to identify, corroborate and address, as appropriate, trade-related concerns and distortions in the global steel market. Through the NASTC, the United States also continued working with the governments of Canada and Mexico to enhance compatibility of the steel import monitoring systems maintained by all three NAFTA countries. These efforts culminated in the launch of a NAFTA Steel Import Monitor in August 2007, which allows online public access to consolidated steel trade data from the United States, Canada and Mexico. The NAFTA Steel Monitor is available at www.NASTC.org.

The continued growth of China's steel production remained a major focus for the United States and other global steel producers in 2007. In December 2005, the United States and China agreed to a cooperative dialogue under the auspices of the JCCT, led by Commerce and USTR on the U.S. side, and by the Ministry of Commerce on the Chinese side. This dialogue represents an effort to increase Chinese government and industry understanding of market-oriented behavior and the problems that subsidies and other government intervention in the steel sector can cause in world steel markets. This dialogue held its third meeting in August of 2007 in Washington, DC, with an agenda that included presentations and discussions on steel market developments, consolidation, steelmaking raw materials, and government support policies. Steel industry representatives from both countries participated in the meeting. The Chinese delegation, which numbered 40 officials, included the National Development and Reform Commission, the Chinese agency responsible for steel industrial policies.

The United States continues to raise specific concerns with other countries bilaterally, at the OECD and in WTO accession negotiations, about steel policies that contribute to excess capacity and production, including subsidies, border measures on steel and steelmaking raw materials, and other trade-distorting practices. The United States also continues its policy of opposing both multilateral and bilateral support for projects that increase raw or finished steel capacity.

MONITORING AND ENFORCEMENT

A. ADVOCACY EFFORTS

1. Monitoring Subsidy Practices Worldwide

Identifying, researching and evaluating potential foreign government subsidy practices is a core function of the Subsidies Enforcement Program. This work is primarily conducted by experienced analysts in IA and involves daily searches of worldwide business journals, periodicals, news publications, as well as online resources maintained by governments, industries and international organizations. Analysts fluent

in a variety of foreign languages, including Chinese, French, Spanish, and German also conduct research in their language of expertise. These analysts are supported by experienced foreign service nationals working with IA staff based in Seoul, South Korea and Beijing, China. Information is also obtained from U.S. embassies overseas through USTR and IA requests for in-depth country-related research. IA research activities are also aided by ongoing relationships with U.S. industry contacts, both in the United States and overseas. USTR and IA staff continued to expand their activities to monitor market- and trade-distorting practices by governments worldwide in 2007, including the provision by governments of harmful subsidies. The information and analysis that is collected from these research activities is a valuable resource to USTR and Commerce in assisting U.S. workers and industries facing competitive pressure from unfair foreign government subsidies.

2. Counseling U.S. Industry

USTR and IA regularly work with U.S. companies concerned with the subsidization of foreign competitors. The goal is to resolve problems through a combination of informal and formal contacts. The United States will also advise U.S. companies of other options, such as a CVD investigation, WTO dispute settlement or an action taken under Section 301 of the Trade Act of 1974.

In 2007, U.S. companies from an array of industry sectors sought assistance on subsidy-related concerns. USTR and IA worked closely with the affected companies to collect information concerning the potential subsidies and to determine how their commercial interests may have been harmed. While companies facing subsidized competition can usually provide good information as to the financial health of their industry, assistance is often needed to obtain additional information regarding the alleged subsidy practices in question. In these instances, USTR and IA 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. USTR and IA also draw upon additional internal and external sources to develop information concerning potentially harmful foreign subsidies. These include Commerce/ITA offices with country and industry specialists that routinely collect information on regional or sector-specific subsidies.

Working with an interagency team, USTR and IA analyze the information and determine the most effective way to proceed. It is often advantageous to pursue resolution of these problems, for example, by raising the matter with the foreign government authorities through informal contacts, formal bilateral meetings or through discussions in the WTO Subsidies Committee. This process may produce more expeditious and practical solutions to the problem than resorting to WTO dispute settlement or the filing of a CVD petition. These contacts may also lead to additional information about the practice in question and affect the decision concerning the

appropriate measures to take. If these efforts fail to adequately resolve the issue, however, bringing a formal dispute settlement action in the WTO always remains an option.

During 2007, USTR and Commerce worked with a broad array of U.S. industries and companies that had significant concerns about unfair foreign government subsidy practices in a wide range of countries. These activities included new and ongoing work on behalf of the U.S. chemical, textile, steel, aerospace, paper, and aluminum industries, to name a few. The subsidy practices examined included those maintained by the central and local governments of Australia, Brazil, Canada, China, the European Union, India, Indonesia, Japan, Mexico, South Korea, Turkey and the UAE.

3. Outreach Efforts

USTR and IA work closely with U.S. government personnel who have constant contact with the U.S. exporting community, both in the United States and abroad, to make them aware of the resources and services available regarding subsidy enforcement efforts. As noted, senior IA officers have been stationed in Beijing, China and Seoul, South Korea, as mandated by Congress. Working closely with their colleagues in U.S. Embassies and IA personnel in Washington, these officers have proved invaluable in undertaking primary source research of potential unfair trade problems in their host countries and in other countries in the region. Overseas personnel have also been an important part of the outreach of the U.S. Government, as they have participated in numerous trade-related seminars in their host countries, which normally cover a country's subsidy-related obligations under the WTO. Additionally, a senior IA officer stationed in Geneva, Switzerland has been a key participant in the Rules negotiations, dispute settlement activities and the WTO Antidumping and Subsidies Committees.

IA personnel also maintain close contacts with other units within Commerce's International Trade Administration (ITA) through the Compliance Coordinators Group (CCG). The CCG is comprised of all of ITA's units (Market Access and Compliance, Manufacturing and Services, Import Administration, and the United States and Foreign Commercial Service (USFCS)), as well as the Patent and Trademark Office. The CCG serves as the central coordinating point for ITA's market access and agreement compliance activities. The group meets regularly to share information on 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. The USFCS, which is charged with counseling U.S. companies through its network of domestic and foreign posts, draws upon SEO resources to inform other USFCS officers and the U.S. business community of the work done, and services offered by the SEO. IA personnel also benefit from information provided by USFCS officers about the types of subsidy problems U.S. companies are facing in their host countries.

USTR and IA work closely with the other U.S. Government agencies, including the Department of State and the U.S. Department of Agriculture, to involve economic and agriculture officers in subsidies enforcement activities.¹⁴ To this end, USTR and IA personnel train State officers on how to identify and evaluate foreign subsidy practices. Cooperation of this type occurs not only when initiated by IA or USTR, but on an ongoing basis whereby State economic officers develop and share information with Commerce, USTR and the interagency team concerning foreign government subsidy practices and the administration of foreign governments' unfair trade laws.¹⁵ This collaboration among government agencies is critically important to help exercise effectively U.S. rights under the Subsidies Agreement.

In 2007, IA organized and participated in many technical exchanges on trade remedies with foreign government officials from Canada, China, Egypt, India, Mexico, Pakistan, South Africa, South Korea, Thailand and Vietnam. These technical exchanges promote a better understanding of other countries' trade remedy practices and allow a more fulsome evaluation of how other countries are complying with their WTO obligations. Technical exchanges have also provided the opportunity to encourage "best practices" and strengthen ties with other trade remedy administrators while fostering increased transparency.

4. Electronic Subsidies Enforcement Library

The 'Electronic Subsidies Enforcement Library' (ESEL) website is a key tool used by IA to organize subsidy-related material and convey it to the public. The website, available at <http://ia.ita.doc.gov/esel/>, is used by USTR, IA, and other Commerce staff to review foreign governments' subsidies notifications made to the WTO, present an overview of the SEO, provide a link to the Subsidies Agreement, and furnish an easily navigable tool which provides information about each subsidy program investigated by Commerce in CVD cases since 1980. (See, Attachment 3.) Another useful aspect of the ESEL is the links it provides to other U.S. and foreign government websites such as USTR, the U.S. Export-Import Bank, the International Monetary Fund, the WTO (which maintains databases of Members' CVD actions, and their subsidy notifications to the

¹⁴ Section 281(g) of the URAA requires that Commerce secure the cooperation of other federal agencies in these activities.

¹⁵ 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, the 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.

WTO), the Canadian and Mexican government trade agencies and the NAFTA secretariat. The website is updated to provide the most recently available information to the public in a timely manner.

B. CHINA

1. World Trade Organization

a. Dispute Settlement

In 2007, the Administration demonstrated its strong commitment to challenge China's trade-distorting subsidies, including at the WTO, when serious dialogue failed to yield the necessary results. Through a series of high-level bilateral meetings in Beijing beginning in 2006, the United States made clear that China needed to withdraw both the prohibited subsidies that it had notified to the WTO Subsidies Committee and several additional apparently prohibited subsidies that it had not notified. The subsidies at issue benefited a wide range of industries in China and included both export subsidies, which make it more difficult for U.S. manufacturers to compete against Chinese manufactured goods in the U.S. market and third-country markets, and import substitution subsidies, which make it more difficult for U.S. manufacturers to sell their products in China.

By February 2007, it had become clear that continued bilateral dialogue would not resolve this matter, and the United States, together with Mexico, initiated WTO dispute settlement proceedings against China. Joint consultations were subsequently held in Geneva in March 2007 and then in June 2007. In July 2007, the United States and Mexico filed requests for the establishment of a WTO panel to hear the dispute, and a panel was established at the August 2007 meeting of the WTO's Dispute Settlement Body. Three months later, in November 2007, the parties to the dispute reached a settlement in which China agreed to eliminate all of the subsidies at issue by January 1, 2008, and not to reinstate them.

Under the terms of the Memorandum of Understanding (MOU) between the United States and China, U.S. companies and workers will benefit from the removal of China's trade-distorting subsidies much sooner than would have been possible if the United States had litigated this case to its conclusion. At the same time, if for any reason China does not meet its MOU commitments, the United States has the right to re-start WTO proceedings. This outcome demonstrates that serious dialogue and resolute enforcement can deliver real results, representing a victory for U.S. manufacturers and their workers.

b. Transitional Review Mechanism (TRM)

In October 2007, the United States took part in the sixth annual transitional review with respect to China's implementation of its WTO obligations. This review is mandated by paragraph 18 of Part I of the Protocol of Accession of the People's Republic of China to the WTO, which provides that all subsidiary bodies, including the Subsidies Committee, "which have a mandate covering China's commitments under the WTO Agreement or [the] Protocol shall, within one year after accession . . . review, as appropriate to their mandate, the implementation by China of the WTO Agreement and of the related provisions of [the] Protocol." Paragraph 18 further states that such reviews shall be conducted on an annual basis for eight years, with a final review occurring by the tenth year after accession.

Upon its accession to the WTO, China agreed to assume the obligations of the WTO Subsidies Agreement, which addresses the use of CVD measures by individual WTO Members and a government's use of subsidies and the application of remedies through enforcement proceedings at the WTO. As part of its accession agreement, China committed that it would eliminate, by the time of its accession, all subsidies prohibited under Article 3 of the Subsidies Agreement, *i.e.*, subsidies contingent on export performance (export subsidies) and subsidies contingent on the use of domestic over imported goods (import substitution subsidies). This commitment expressly extended throughout China's customs territory, including in special economic zones and other special economic areas. The Subsidies Agreement also requires that China, like all other WTO Members, notify all of its subsidies, as defined by Article 25 of the Agreement, maintained by the national and all sub-national governments.

China also agreed to various special rules that apply when other WTO members seek to enforce the disciplines of the Subsidies Agreement against Chinese subsidies (either in individual WTO Members' CVD proceedings or in WTO enforcement proceedings). Under these rules, in certain circumstances, WTO Members can identify and measure Chinese subsidies using alternative methods in order to account for the special characteristics of China's economy. For example, when determining whether preferential government benefits have been provided to a Chinese enterprise via, for example, a loan, under certain conditions WTO members can use foreign or other market-based criteria rather than Chinese benchmarks to ascertain the benefit of that loan and its terms. Special rules also govern the actionability of subsidies provided to state-owned enterprises (SOEs).

As previously reported, following increasing pressure from the United States and other WTO members, China finally submitted its long-overdue subsidies notification to the WTO's Subsidies Committee in April 2006. Although the notification reported on more than 70 subsidy programs, it was also notably incomplete, as it failed to notify any subsidies provided by China's state-owned banks or by provincial and local government

authorities. This failure leaves a significant gap in China's subsidies reporting and is particularly troubling given the important role played by sub-national governments in China's banking system and in the development of Chinese industry. (For further information see, *WTO Subsidies Committee, Subsidy Notifications*, section below). More generally, in the course of the TRM as conducted by the WTO Subsidies Committee, the United States raised subsidy issues with respect to: (1) China's textile and steel industries; (2) state-owned bank and state-owned asset management company practices; and (3) government support policies for the restructuring of state-owned enterprises in China's northeast regions.

In 2008, the United States will continue to research and analyze possible Chinese subsidy programs. At the WTO, using both regular meetings and transitional reviews before the Subsidies Committee, U.S. engagement will focus on the need for China to eliminate any remaining subsidies prohibited under the Subsidies Agreement – including those at the sub-national level – and to adhere more fully to its subsidy reporting obligations.

2. Application of Countervailing Duty Law to China

Many U.S. industries, including the steel, paper and textiles industries, among others, continued to express concern about the trade-distorting effects of various Chinese subsidies. These concerns led to the U.S. paper industry's filing of a petition with Commerce in October 2006 requesting the initiation of a CVD investigation based on allegations of subsidized imports of coated free sheet paper from China causing injury in the U.S. market. The petition requested a change to Commerce's longstanding policy of not applying U.S. CVD law to China or any other country considered a "non-market economy" for antidumping purposes. Commerce initiated an investigation in November 2006, and during the course of the ensuing investigation it changed its policy and began applying U.S. CVD law to China after finding that reforms to China's economy in recent years had removed the obstacles to applying the CVD law that were present in the "Soviet-era economies" at issue when Commerce first declined to apply the CVD law to non-market economies in the 1980s. In its final determination, issued in October 2007, Commerce found that China's paper industry benefitted from a wide range of countervailable subsidies.¹⁶ Several other U.S. industries concerned about subsidized Chinese imports have filed CVD petitions in 2007. In 2007, Commerce initiated CVD investigations of steel pipe, laminated woven sacks, tires, magnets, thermal paper and sodium nitrite imports from China. These cases are scheduled to be completed in 2008.

The subsidies Commerce investigated in the coated free sheet paper case, and those alleged and currently being examined in the ongoing proceedings listed above,

¹⁶ As noted above, Commerce did not issue a final countervailing duty order in this case, because the ITC found no injury to the U.S. industry.

include preferential policy loans, income tax and VAT exemptions and reductions, the provision of goods and services on non-commercial terms, and a variety of provincial and local government subsidies. Given some of the unique features of China's economy, a number of the subsidies investigated in these cases present novel and complex issues, from both a legal and methodological perspective.

One example is policy lending by Chinese banks, including state-owned commercial banks. In the paper case, Commerce found that banks in China provided loans to the paper sector pursuant to central government policies favoring that industry. Commerce further determined that because of significant distortions in the Chinese banking sector, loans from Chinese banks could not serve as a benchmark to determine the subsidy benefit, if any. Therefore, for its benefit calculation, Commerce compared the interest rates on the government loans in China to interest rates on loans in certain third-countries. Specifically, Commerce used an average rate based on interest rates, adjusted for inflation and "quality of institutions", in countries with similar per capita gross income (GNI) to China. Commerce concluded in the paper case that this average captured the broad inverse relationship between GNI and interest rates.

Commerce will continue to devote all the necessary resources to the many novel and complex issues presented in its ongoing proceedings, including, for example, allegations of the government provision of goods and services on non-commercial terms, and a number of local and provincial level subsidies.

Commerce's decision to apply the U.S. anti-subsidy law to imports from China represents the first application of the U.S. countervailing duty law to imports from a non-market economy. The decision alters a 23-year old policy of not applying the CVD law to non-market economy countries. Applying the U.S. CVD law to potentially injurious subsidized imports from China demonstrates the Administration's commitment to leveling the playing field for American companies, workers and farmers.

3. JCCT - Structural Issues Working Group (SIWG)

Established in 1983, the JCCT is a government-to-government consultative mechanism that provides a forum to resolve trade concerns and promote bilateral commercial opportunities. The status of the JCCT was elevated following the December 2003 meeting of President Bush and Chinese Premier Wen to focus higher-level attention on outstanding trade disputes. It is chaired by Secretary Gutierrez and Ambassador Schwab on the U.S. side and by Vice Premier Wu Yi on the Chinese side.

In the case of China, one approach to address existing market and trade distortions is to encourage China's ongoing structural reforms, which are intended to create a market economy. At the same time, China's treatment as a non-market

economy under U.S. antidumping law is of substantial concern and importance to the Chinese government. In order to better understand China's reforms to date and various structural and operational aspects of China's economy, as well as to discuss issues that relate to China's desire for market economy status under the U.S. antidumping law, China and the United States agreed during the April 2004 JCCT meetings to the establishment of a new working group, the SIWG, to be jointly chaired by Commerce's Assistant Secretary for Import Administration and the Assistant U.S. Trade Representative for China Affairs on the U.S. side and the Director General of the Bureau of Fair Trade from China's Ministry of Commerce (MOFCOM) on the Chinese side.

The United States attaches great importance to the SIWG. It provides a forum for the U.S. and Chinese governments to explore and discuss China's economy and its ongoing economic reform program, pragmatically address concerns about market- and trade-distorting practices that might otherwise lead to bilateral trade frictions, and consider the Government of China's concerns about China's nonmarket economy (NME) status under U.S. antidumping law.¹⁷ The working group has met a number of times since its launch in July 2004, with both sides including in their delegations experts from a variety of agencies responsible for the broad range of structural/institutional issues and economic reforms/policies under discussion. During the July 2005 meeting of the JCCT, China and the United States agreed to intensify the SIWG process to provide greater opportunity to explore with China its economic policies and reforms at a more technical level. In addition, the United States made it a priority to directly address subsidies in the SIWG and obtained Chinese government agreement to do so.

In the inaugural meeting of the U.S.-China Strategic Economic Dialogue in December 2006, both China and the United States agreed to invigorate discussion under the JCCT of structural issues/market economy status, with the SIWG providing the vehicle for doing so. To that end, the United States has been working with China to schedule a next meeting of the working group to follow up on the constructive discussions held in April 2007.

¹⁷ In December 2005, a Chinese company, with the support of the Chinese government, requested a review of China's NME status in the antidumping investigation of certain lined paper products. Commerce issued its full analysis of China's economy in August 2006, finding that China remains an NME for purposes of the U.S. antidumping law. In considering this request for a review of China's NME status, Commerce took note of the economic reforms that China had implemented to date, as well as the significant areas of China's economy where, it is generally recognized, fundamental reforms remain incomplete, e.g. the banking sector, land ownership and property rights, and the rule of law. The SIWG is not a forum for resolving this issue, but it provides a constructive setting for the mutual exchange of views and relevant information. Under U.S. law, any review of China's NME status must take place in a formal proceeding before Commerce, open to all interested parties.

C. WTO DISPUTE SETTLEMENT AND CVD CASES OF SIGNIFICANCE TO SUBSIDIES DISCIPLINES

1. European Union Support for Airbus

For many years, the United States has had serious concerns about the continued EU subsidization of Airbus, a company with more than a 50 percent share of the world market for large civil aircraft ("LCA"). The subsidies have taken many forms, including "launch aid," which Airbus uses to launch new models of aircraft; grants for Airbus infrastructure; forgiveness of debt; and subsidies to underwrite Airbus' research and development costs.

U.S. concerns about Airbus subsidies intensified in 2004, when it became apparent that Airbus intended to launch a new aircraft, the A350, with another round of EU launch aid. In October 2004, following unsuccessful, U.S.-initiated efforts to negotiate a new U.S.-EU agreement that would preclude new subsidies, the United States filed a WTO consultation request with respect to the A350 subsidies and other subsidies that Airbus has received. Concurrent with the U.S. WTO consultation request, the United States also exercised its right to terminate the 1992 U.S.-EU bilateral LCA agreement.

The WTO consultations failed to resolve the U.S. concerns, and a renewed effort to negotiate a solution ended without success in April, 2005. Therefore, on May 31, 2005, the United States filed a WTO panel request. The WTO established a panel on July 20, 2005, and panel proceedings are currently ongoing. (Separately, also on May 31, 2005, the EU filed a WTO panel request with respect to alleged U.S. federal, state and local government subsidies to Boeing. The EU's complaint is pending before a different WTO panel.) The parties have filed several written submissions, and the panel heard arguments by the parties at meetings in March and July 2007. The panel's original timetable has been revised, and a new date for issuance of the panel's report has not been set.

U.S. officials have consistently noted their willingness to negotiate a new bilateral agreement on large civil aircraft, even while the WTO litigation proceeds, but have insisted that any such agreement must end launch aid and other direct subsidies for the development and production of such aircraft.

2. United States Support for Upland Cotton

On September 8, 2004, the panel in *United States—Subsidies on Upland Cotton* circulated its final report. The panel, *inter alia*, made the following findings: (1) certain export credit guarantees (GSM 102, GSM 103, SCGP programs) were prohibited export subsidies; (2) some U.S. domestic support programs (marketing loan, counter-cyclical, market loss assistance, and Step 2 payments) were found to cause significant suppression of cotton prices in the world market causing serious prejudice to Brazil's interests; (3) other U.S. domestic support programs (production flexibility contract payments, direct payments, and crop insurance payments) did not cause serious prejudice to Brazil's interests because the programs were not shown to cause significant price suppression; and (4) Step 2 payments to exporters of cotton were prohibited export subsidies and Step 2 payments to domestic users were prohibited import substitution subsidies because they were contingent upon the purchase of U.S. cotton.

The United States and Brazil appealed several of the panel's findings. The Appellate Body circulated its report on March 3, 2005, upholding the panel's findings appealed by the United States. The Appellate Body also rejected or declined to rule on most of Brazil's arguments. On March 21, 2005, the WTO's Dispute Settlement Body (DSB) adopted the panel and Appellate Body reports and, on April 20, 2005, the United States advised the DSB that it intended to bring its measures into compliance.

On June 30, 2005, the United States announced that it would cease to issue export credit guarantees under the GSM 103 program. It also announced a new fee structure for the GSM 102 program designed to make the program more "risk-based," consistent with the original panel's findings. The United States ceased to issue guarantees under the SCGP as of October 1, 2005.

On July 5, 2005, the United States proposed legislation to, *inter alia*, repeal the Step 2 program. The repeal was adopted by Congress on February 1, 2006, with an effective date of August 1, 2006.

On July 5, 2005, Brazil requested authorization to impose countermeasures and suspend concessions in the amount of \$3 billion in connection with the "prohibited subsidy" findings. On July 14, 2005, the United States objected to the request, thereby referring the matter to arbitration. On August 17, 2005, the United States and Brazil agreed to suspend the arbitration. On October 6, 2005, Brazil made a separate request for authorization to impose countermeasures and suspend concessions in the amount of \$1 billion per year in connection with the "serious prejudice" findings. The United States objected to Brazil's request on October 17, 2005, and that matter was also referred to arbitration. Thereafter, on November 21, 2005, the United States and Brazil jointly requested suspension of this second arbitration.

On September 28, 2006, the Dispute Settlement Body established an Article 21.5 (compliance) panel, at Brazil's request, to review U.S. compliance with the rulings in the dispute. Brazil argued that the United States remained out of compliance with both the prohibited subsidy findings and the actionable subsidy findings. The compliance panel issued its final report to the parties on October 15, 2007. The final report was circulated to WTO Members on December 18, 2007. The panel found, *inter alia*, that: (1) export credit guarantees issued under the GSM 102 program with respect to unscheduled and certain scheduled (rice, pig and poultry meat) commodities constituted prohibited export subsidies; and (2) U.S. marketing loan and counter-cyclical payments for upland cotton were continuing to cause serious prejudice to Brazil by significantly suppressing world upland cotton prices. The panel rejected Brazil's claim that payments under the marketing loan and counter-cyclical payment programs were responsible for an increase in U.S. market share in MY 2005 and thereby caused serious prejudice to Brazil's interests. The panel also agreed that the United States was not required to have refused to perform on export credit guarantees that were issued prior to the deadline for the implementation of the DSB's recommendations and rulings as to such guarantees (July 1, 2005) and that were still outstanding as of that date.

The United States and Brazil now have the option of appealing the compliance panel's report. As of the date of publication, the deadline for the appeal (no later than February 16, 2008) had not yet lapsed.

3. Canada - U.S. Softwood Lumber Agreement

The Canada - U.S. Softwood Lumber Agreement was signed on September 12, 2006, and entered into force on October 12, 2006. On October 12, pursuant to a settlement of litigation, the Department of Commerce revoked the antidumping and countervailing duty orders on imports of softwood lumber from Canada. The revocations were effective retroactive to May 22, 2002 (the day the orders originally went into effect), and there is no possibility of reinstatement. Upon revocation of the orders, U.S. Customs and Border Protection (CBP) ceased collecting cash deposits, and began returning all previously-collected deposits, with interest (approximately US\$5.5 billion), to the importers of record. At the time of entry into force, there was an injunction preventing liquidation of entries covered by the first administrative review, but the U.S. Court of International Trade subsequently lifted the injunction on October 27, 2006 in order to permit liquidation of those entries. Liquidation was completed in mid-January 2007. Pursuant to a Settlement of Claims Agreement, the United States, Canada, and certain private litigants agreed to terminate, or take steps to terminate, much of the litigation over trade in softwood lumber.

Under the terms of the Agreement, when lumber prices decline to a certain level, Canadian exporting provinces can choose either to collect an export tax that ranges from 5 to 15 percent as prices fall, or to collect lower export taxes in return for export

volume limits. If softwood lumber prices rise above \$355 per thousand board feet, imports from Canada are unrestricted. Certain softwood lumber products are excluded from the border measure: (1) softwood lumber made from logs harvested in the Maritimes provinces (New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador); (2) softwood lumber made from logs harvested in the Yukon or Northwest Territories, or Nunavut; and (3) softwood lumber manufactured by one of 32 named companies, primarily located in Quebec (largely “border mills” that source most of their logs from Maine). The Agreement also includes provisions to address potential import surges from Canada, provide for effective dispute settlement, and discipline future trade cases.

The Agreement establishes a bi-national working group to discuss Canadian provincial policy reforms regarding timber pricing and a Softwood Lumber Committee. The bi-national working group will develop substantive criteria and procedures for exempting certain exports of softwood lumber from the export measures discussed above, if and when a region in Canada reforms its public timber system so that it uses market-determined timber pricing and forest management systems. This group will also serve as a forum for resolving concerns between the parties regarding timber pricing and forest management systems. USTR has the lead in implementing and overseeing the Agreement on behalf of the United States, with ITA, U.S. Customs and Border Protection, and Census playing significant roles as needed to provide expertise. The Softwood Lumber Committee will supervise the implementation of the Agreement, supervise working groups related to the Agreement, and consider any other matters that affect the Agreement.

Under the SLA’s Anti-circumvention provision (Article 17), Canada agreed to not take any action to reduce or offset the export measures called for by the Agreement. However, Quebec and Ontario have put in place several assistance programs that we believe violate the Agreement’s Anti-circumvention provisions. These include several grant, loan, loan guarantee, and tax credit programs, as well as “forest management” programs and programs that promote wood production. The United States requested consultation on these programs on March 30, 2007. Those consultations did not lead to a resolution of the dispute, and the United States requested arbitration on January 18, 2008, under London Court of International Arbitration rules. Following the request for arbitration, there is an approximately two-month process to select the arbitrators, and pursuant to the SLA the arbitral tribunal is to issue its award within six months of its appointment.

4. Canadian Countervailing Duty Investigation of Grain Corn from the United States

On September 16, 2005, the Canada Border Services Agency (CBSA) initiated antidumping and CVD investigations on grain corn originating in or exported from the United States. Preliminary duties were imposed from December 15, 2005. However, on April 18, 2006, the Canadian International Trade Tribunal (CITT) made a finding of no injury, resulting in the termination of the investigations and a full refund of all preliminary duties. Throughout the CVD investigation, USTR, Commerce and the Department of Agriculture strongly defended the interests of the U.S. corn industry. These efforts included providing factual information to the Canadian authorities, providing written arguments to the CBSA and CITT, and participating in verification meetings in Washington.

On June 7, 2006, three Canadian provincial corn producer associations appealed the final CITT no-injury determination to Canada's Federal Court of Appeal. The United States submitted a brief to the court on December 4, 2006. On June 5, 2007, immediately following oral argument, the court unanimously rejected the appeal and affirmed the CITT determination. The court's decision definitively ended this proceeding. Accordingly, the binational panel review under Chapter 19 of the North American Free Trade Agreement of the final CBSA subsidy determination, which had been requested by several Canadian corn importers, was dismissed as moot with the consent of all parties.

5. United States Domestic Support for Agriculture

On January 8, 2007, Canada requested WTO dispute settlement consultations with the United States, alleging that: (1) support to U.S. corn producers has caused and threatens to cause serious prejudice to the interests of Canada, specifically through price suppression in the Canadian corn market; (2) U.S. export credit guarantee programs for corn and all unscheduled commodities constitute prohibited export subsidies; and (3) that U.S. government support for all agricultural products resulted in a breach of the U.S. scheduled cap on its Aggregate Measure of Support (AMS) under the Agreement on Agriculture. On July 11, 2007, Brazil submitted a request for consultations that made claims similar to the second and third allegations made by Canada.

On November 8, 2007, both Canada and Brazil requested the establishment of a panel, limited to the claims that total U.S. support for agriculture breached the U.S. AMS limit in each of 1999, 2000, 2001, 2002, 2004, and 2005, contrary to the Agreement on Agriculture. More than 100 programs were identified in each panel request as allegedly providing support during the relevant years. The panel request did not include claims under the SCM Agreement that had been part of the consultations request (*i.e.*, serious prejudice with respect to corn and export credit guarantee programs). The panel was established by the WTO DSB on December 17, 2007.

D. WTO SUBSIDIES COMMITTEE

The Subsidies Committee's agenda in 2007 included its routine activities concerned with reviewing and clarifying the consistency of WTO Members' domestic laws, regulations and actions with Agreement requirements. During the fall meeting, the Committee undertook its sixth annual transitional review with respect to China's implementation of the Agreement (see, *Transitional Review Mechanism* section above). Other issues addressed in the course of the year included: a further extension of the transition period for the phase-out of export subsidies for certain developing country Members, the examination of specific export subsidy program extension requests, the updating of the methodology for Annex VII (b) of the Agreement and consideration of new members for the Permanent Group of Experts. Further information on these various activities is provided below.

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 Subsidies Agreement. In keeping with the objectives and directives expressed in the URAA, WTO subsidy notifications also play an important role in the United States' monitoring and enforcement activities under the Subsidies Agreement.

Under Article 25.2 of the Subsidies 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. In 2007, seven 2005 new and full subsidy notifications and four 2007 new and full notifications were reviewed.¹⁸ Unfortunately, numerous Members have never made a subsidy notification to the WTO, although many are lesser developed countries.¹⁹

Perhaps most importantly, as noted previously, the Committee continued its examination of the new and full notification of China's subsidies to the WTO, which was originally submitted in April 2006. The United States has devoted significant time and

¹⁸ The 2005 new and full notifications of the following Members were reviewed by the Committee in 2007: Argentina; Chile; Honduras; Liechtenstein; Tunisia; Suriname and Swaziland. The Committee continued its review of the 2005 new and full notifications of the following Members: China; Hong Kong, China; Korea; New Zealand; Singapore; Qatar; Thailand and Turkey. The Committee also reviewed the 2007 new and full notifications of the following Members: Armenia; Honduras; Macao, China and Nigeria.

¹⁹ For further information, see the Report (2007) of the WTO Committee on Subsidies and Countervailing Measures (G/L/840; November 12, 2007).

resources to monitoring and analyzing China's subsidy practices, and these efforts helped to identify promptly significant omissions in China's subsidy notification. In accordance with the Subsidies Committee procedures, the United States submitted extensive written questions and comments on China's subsidies notification in July 2006, as did several other WTO Members, including the EC, Japan, Canada, Mexico, Australia and Turkey. Although China responded in writing to these submissions in the fall of 2007, little information was provided with respect to subsidies provided by China's state-owned banks and asset management companies, and sub-national government authorities. Other program-specific answers were often inadequate to permit a reasonable understanding of the programs at issue. USTR and IA staff will aggressively continue to work together to address these unresolved issues.

While not reviewed in the 2007 Committee meetings, the United States submitted its 2005 new and full subsidies notification in October 2007. 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 requiring a significant commitment of staff and other resources of both USTR and Commerce. The U.S. subsidy notification submitted in 2007 included over 40 federal programs and a substantial increase in the number of state programs notified – 390 in total. This reflected an intensified research effort and heightened cooperation between federal and state government personnel. As such, this notification reflected the further institutionalization of the U.S. WTO subsidy notification process.

2. Review of CVD 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 laws and regulations and their relationship to the obligations of the Agreement. The United States continued to play an important 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, 87 Members of the WTO (counting the current 27 Members of the European Union as one) have notified that they have CVD legislation in place, or have notified that they have no such legislation, while 35 Members have not made a notification. Among the notifications of CVD laws and regulations reviewed in 2007 were those of Albania, Japan, Nigeria and the United States.

As for CVD measures, five WTO Members notified CVD actions taken during the latter half of 2006, and six Members notified actions taken in the first half of 2007.

Specifically, the Committee reviewed actions taken by Australia, Brazil, Canada, Chile, the European Union, and the United States.

3. Article 27.4 Update

Under the SCM Agreement, most developing country Members were obligated to eliminate their export subsidies by December 31, 2002. Article 27.4 of the SCM Agreement allows for the SCM Committee to grant an extension of this deadline provided certain conditions are met. If the Committee does not affirmatively sanction a continuation, the export subsidies must be phased out within two years.

To address the concerns of certain small developing country Members, a special procedure within the context of Article 27.4 of the SCM Agreement was adopted at the Fourth Ministerial Conference in 2001. Members meeting all the qualifications for the agreed-upon special procedures were eligible for annual extensions for a five-year period through 2007, in addition to the two years referred to under Article 27.4. Antigua and Barbuda, Barbados, Belize, Costa Rica, Dominica, Dominican Republic, El Salvador, Fiji, Grenada, Guatemala, Jamaica, Jordan, Mauritius, Panama, Papua New Guinea, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Uruguay have made yearly requests since 2001 under these special procedures.²⁰ These requests were approved by the SCM Committee each year.

In April 2006, the Members which benefited from the special procedures agreed to in 2001, requested a further extension through the year 2018. After numerous informal meetings, the SCM Committee decided to recommend to the General Council that it extend the transition period until 2013 under similar special procedures as previously, with a two-year phase-out period ending 2015. An important outcome of these negotiations, insisted upon by the United States and other developed and developing countries, was that the beneficiaries have no further recourse to extensions beyond 2015. The SCM Committee also decided to recommend that the lesser developed countries that have not graduated from Annex VII of the SCM Agreement and that participated under the earlier special procedures be allowed to take advantage of the extension from the date of graduation through the available remaining period. The General Council adopted the recommendation of the SCM Committee in July 2007.

Specific export subsidy program extension requests under the newly agreed upon procedures were made in 2007 by all of the developing country Members listed above. These requests required, *inter alia*, a detailed examination of whether the

²⁰ Bolivia, Honduras, Kenya, and Sri Lanka are all listed in Annex VII of the SCM Agreement and thus, may continue to provide export subsidies until their “graduation”. Therefore, these Members only reserved their rights under the special procedures in the event they graduated during the five-year extension period contemplated by the special procedures.

applicable standstill and transparency requirements had been met. In total, the SCM Committee conducted a detailed review of more than 40 export subsidy programs. At the end of the process, all of the requests under the new special procedures were granted. (A chart of all the programs is found in Attachment 4.)

E. U.S. MONITORING OF SUBSIDY-RELATED COMMITMENTS

1. Accessions

Countries and separate customs territories seeking to join the WTO must negotiate the terms of their accession with current Members. In a typical accession negotiation, the applicant submits an application to the WTO General Council, which establishes a Working Party to review information on the applicant's trade regime and to oversee the negotiations. Accession negotiations involve a detailed review of the applicant's entire trade regime by the Working Party and bilateral negotiations for import market access.

The economic and trade information reviewed by the Working Party includes the acceding candidate's subsidies regime. USTR and Commerce, along with an interagency team, review the compatibility of acceding parties' subsidy regimes with WTO subsidy rules. Specifically, information on the nature and extent of the candidate's subsidies is examined, with particular emphasis on subsidies that are prohibited under the Subsidies Agreement. Additionally, an accession candidate's trade remedy laws are examined to determine their compatibility with the relevant WTO obligations.

Subsidy-related information is summarized in a memorandum submitted by an applicant detailing its foreign trade regime, which is supplemented and corroborated by independent research throughout the accession negotiation. The United States' policy is to seek commitments from accession candidates that they eliminate all prohibited subsidies upon joining the WTO, and that they will not introduce any such subsidies in the future. Additional commitments may be sought regarding any subsidies that are of particular concern to U.S. industries.

In 2007, WTO accession negotiations continued with a wide range of countries that, to varying degrees, included discussion of these countries' subsidies regimes. These include Ukraine, Russia, Cape Verde, Tonga, Algeria, among others. For example, in December 2007, the Working Party on Cape Verde's accession adopted Cape Verde's accession package. As a least developed country (LDC), Cape Verde is entitled to more flexible terms of WTO accession, with transitions for implementation of

its obligations, and market access terms that take account of its unique economic

limitations. With regard to subsidies, Cape Verde agreed to cease granting subsidies deemed prohibited under the Subsidies Agreement within two years.

Tonga also ratified its accession package on 27 June 2007, which included a commitment not to maintain subsidies prohibited under Article 3 of the Subsidies Agreement from the date of accession. Finally, Ukraine is nearing completion of its accession process. In its bilateral discussions, the United States worked very closely with Ukraine on its subsidy notification to ensure that it met its notification obligations prior to accession. IA staff met with Ukrainian representatives twice in 2007 to provide assistance in this regard. The United States is also working with Ukraine on revising its trade remedy laws to ensure full compliance with the relevant WTO provision upon accession.

2. 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 of: (1) increasing transparency and promoting understanding of other countries' trade policies and practices; (2) improving the quality of public and intergovernmental debate on important issues; and (3) enabling 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.

Trade Policy Reviews (TPRs) focus on the trade policies and practices of a particular country while also taking into account overall economic and developmental needs, policies and objectives, as well as the external economic environment that a country faces. The four largest traders in the WTO (the European Union, the United States, Japan and China) are examined once every two years. The next 16 largest 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.

These reviews play an important role in ensuring that WTO Members meet transparency requirements concerning their subsidy practices. TPRs also provide a broader context than the Subsidies Committee notification reviews in which to assess a Member's subsidy policies and their role in that Member's economy. In reviewing these reports, USTR and Commerce focus on the information concerning the subsidy practices detailed in the report, but also conduct additional research on potential omissions regarding known subsidy practices that have not been reported. In 2007,

USTR and Commerce reviewed 19 Members' TPRs, including those of Australia, the European Union, Japan, India and Thailand.

CONCLUSION

The past year witnessed several seminal events in the enforcement and development of international and national subsidy disciplines. Early in the year, the United States launched its first WTO dispute settlement subsidies proceeding alleging that China was providing subsidies prohibited under the Subsidies Agreement. After months of difficult negotiations, a settlement was reached that required China to completely eliminate these subsidies. This was a notable achievement, not only because it was accomplished without the need to complete lengthy WTO litigation, but also because it demonstrated a clear recognition by China of the existing rules and a serious willingness to come into compliance. 2007 also marked the first year that the U.S. countervailing duty law was applied to imports from a non-market economy, altering a policy of 23 years. While difficult policy issues have been and will continue to be presented in this area, the fundamental decision to change direction was in many ways a recognition of the economic changes that have occurred in China and the need to adjust the administration of the U.S. countervailing duty law accordingly.

Finally, the Chairman of the WTO Rules Group issued a draft text proposing amendments to the existing subsidy rules and an entirely new set of disciplines on fisheries subsidies. While the proposed amendments to the existing rules fall short of the United States' expectations and need to be strengthened, it should not be overlooked that the draft text adopts positions long advocated by the United States and that efforts to weaken the existing rules did not prevail. Most strikingly, however, are the comprehensive fisheries subsidies disciplines proposed, which if ultimately accepted, would represent the strongest sectoral subsidy disciplines to which the international community has ever agreed and a decisive response by the multilateral trading system to the continuing serious and potentially catastrophic problems facing the fisheries of the world.

ATTACHMENT 1

ASSISTING U.S. EXPORTERS TO COMPETE EFFECTIVELY

SUBSIDIES ENFORCEMENT

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 non-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.

- o **Export financing** at preferential rates.
- o **Grants or Tax exemptions** for favored companies or industries.
- o **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").

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:

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ATTACHMENT 2

**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 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/email: trcs@ita.doc.gov

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

- **Sorted by Date**
- **Sorted by Country**

Annual Reports to Congress on Subsidies Enforcement

- **Reports from 1998-2007**
- **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 of this Report, which 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 have been analyzed by Import Administration staff during countervailing duty (CVD) proceedings since 1980. The information is provided by country and then subdivided into various categories, based on the DOC's finding in the proceeding. More detailed information about a 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. As of

December 2007, the number of countries which have had programs investigated in U.S. CVD proceedings was 53.

WTO Subsidies Notifications

This will link the visitor to all unrestricted WTO subsidy notifications, listed either by date or by country. Beside each country's name is a description of the document, the document number and document symbol as well as the date the document was submitted to the WTO. Clicking on the name of a country will lead the visitor to that country's subsidy notification. The notification will provide a list of notified subsidies, in addition to specific information concerning each 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. Although the Subsidies Agreement stipulates that the notification of a subsidy practice does not prejudice 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.

Annual Reports to Congress on Subsidies Enforcement

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

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

**Further 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	Extension granted
	Free Trade/Processing Zones	Extension granted
BARBADOS	Fiscal Incentive Program	Extension granted
	Export Allowance	Extension granted
	Research & Development Allowance	Extension granted
	International Business Incentives	Extension granted
	Societies with Restricted Liability	Extension granted
	Export Re-discount Facility	No extension requested.
	Export Credit Insurance Scheme	No extension requested.
	Export Finance Guarantee Scheme	No extension requested.
	Export Grant & Incentive Scheme	No extension requested.
BELIZE	Fiscal Incentives Program	Extension granted
	Export Processing Zone Act	Extension granted
	Commercial Free Zone Act	Extension granted
	Conditional Duty Exemption Facility	Extension granted
BOLIVIA (Annex VII Country)	Free Zone	Reservation of rights. No action taken.
	Temporary Admission Regime for Inward Processing	Reservation of rights. No action taken.
COSTA RICA	Duty Free Zone Regime	Extension granted
	Inward Processing Regime	Extension granted
DOMINICA	Fiscal Incentives Program	Extension granted
DOMINICAN REPUBLIC	Law No. 8-90, to "Promote the Establishment of Free Trade Zones"	Extension granted
EL SALVADOR	Export Processing Zones & Marketing Act	Extension granted
	Export Reactivation Law	No extension requested.
FIJI	Short-Terms Export Profit Deduction	Extension granted
	Export Processing Factories/Zones Scheme	Extension granted

	The Income Tax Act (Film Making & Audio Visual Incentive Amendment Degree 2000)	Extension granted
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GRENADA	Fiscal Incentives Act No. 41 of 1974	Extension granted
	Qualified Enterprise Act No. 18 of 1978	Extension granted
	Statutory Rules and Orders No. 37 of 1999	Extension granted
GUATEMALA	Special Customs Regimes	Extension granted
	Free Zones	Extension granted
	Industrial and Free Trade Zones (ZOLIC)	Extension granted
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	Extension granted
	Jamaica Export Free Zone Act	Extension granted
	Foreign Sales Corporation Act	Extension granted
	Industrial Incentives (Factory Construction) Act	Extension granted
JORDAN	Income Tax Law No. 57 of 1985, as amended	Extension granted
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	Extension granted
	Pioneer Status Enterprise Scheme	Extension granted
	Export Promotion	Extension granted
	Freeport Scheme	Extension granted
PANAMA	Export Processing Zones	Extension granted
	Official Industry Register	Extension granted
	Tax Credit Certificates (CAT)	No extension requested.
PAPUA NEW GUINEA	Section 45 of the Income Tax Act	Extension granted

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	Extension granted
ST. LUCIA	Fiscal Incentives Act	Extension granted
	Micro & Small Scale Business Enterprise Act	Extension granted
	Free Zone Act	Extension granted
ST. VINCENT AND THE GRENADINES	Fiscal Incentives Act	Extension granted
URUGUAY	Automotive Industry Export Promotion Regime	Extension granted

*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.