H.R. 1229, THE NONMARKET ECONOMY TRADE REMEDY ACT OF 2007

HEARING

BEFORE THE

SUBCOMMITTEE ON TRADE

OF THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

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THURSDAY, MARCH 15, 2007

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON TRADE,
Washington, DC.

The Subcommittee met, pursuant to notice, at 1:03 p.m., in room 1100, Longworth House Office Building, the Honorable Sander M. Levin (Chairman of the Subcommittee) presiding.

[The advisory announcing the hearing follows:]

HEARING ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

Trade Subcommittee Chairman Levin Announces a Hearing on the Nonmarket Economy Trade Remedy Act of 2007

March 7, 2007

By (202) 225–6649

Ways and Means Trade Subcommittee Chairman Sander M. Levin today announced the Trade Subcommittee will hold a hearing on the application of countervailing duties to unfairly subsidized and injurious imports from nonmarket economy countries, with a focus on H.R. 1229, the "Nonmarket Economy Trade Remedy Act of 2007." **The hearing will take place on Thursday, March 15, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 1:00 p.m.**

In view of the limited time available to hear witnesses, oral testimony at this hearing will be from the invited witness only. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

FOCUS OF THE HEARING:

The purpose of the hearing is to examine whether to apply countervailing duties to unfairly subsidized and injurious imports from nonmarket economy countries such as China. It will focus on H.R. 1229, the "Nonmarket Economy Trade Remedy Act of 2007," introduced by Representatives Artur Davis (D–AL) and Phil English (R–PA) on February 28, 2007.

BACKGROUND:

The countervailing duty law provides for the assessment of import duties in an amount equivalent to the amount of the subsidy received on that imported product. For more than 20 years, the U.S. Department of Commerce ("Commerce") has refused to apply the U.S. countervailing duty law to unfairly subsidized and injurious imports from "nonmarket economy" countries such as China. Commerce has reasoned that government intervention in the economy of non-market economy countries is so pervasive that meaningful comparisons between subsidized and market-determined prices are not possible. The Federal Circuit affirmed this practice in 1986 in *Georgetown Steel Corp.* v. *United States.* Under its current practice, Commerce imposes countervailing duties on subsidized and injurious imports only from market economy countries.

In October 2006, a petition was filed requesting the initiation of a countervailing duty investigation, based on allegations of injurious subsidized imports of coated free sheet (CFS) paper from China. On November 21, 2006, Commerce announced its decision to initiate a countervailing duty investigation. (See 71 *Federal Register* 68546, Nov. 27, 2006.) However, according to the Office of the U.S. Trade Representative and Commerce, "[i]n initiating this investigation, Commerce has not decided that the CVD law applies to NME countries. Instead, based on the petitioner's arguments, Commerce has determined that it is appropriate to revisit the question[.]" (See Subsidies Enforcement Annual Report to the Congress, February 2007.) Thus, it remains unclear whether, and how, Commerce intends to apply countervailing duty law to nonmarket economy countries. The Government of China has appealed Commerce's initiation of a countervailing duty investigation to the U.S. Court of International Trade and is requesting a preliminary injunction. The Court has not yet ruled on that request, although it did deny China's motion for a temporary restraining order that would have prevented Commerce's investigation.

The most commercially significant nonmarket economy country is China. U.S. exports to China in the first 11 months of 2006 were more than $50 billion, up from $42 billion in all of 2005, and up from just $19 billion in 2001, the year China acceded to the World Trade Organization ("WTO"). Notwithstanding this substantial growth in U.S. exports, the U.S. goods trade deficit with China in 2006 is expected to approach one-quarter of a trillion dollars—the largest trade deficit in U.S. history. China accounts for roughly 12 percent of total U.S. trade and one third of the total U.S. goods trade deficit with the world. (At the same time, U.S. imports from other East Asian countries have fallen $10 billion between 2001 and 2005.)

It is widely recognized that China has a large number of subsidy programs that distort the Chinese market and trade with the United States. In 2006, China submitted a long-overdue subsidies notification to the WTO. China identified over 70 subsidy programs (including some subsidies that appear to be prohibited under WTO rules), but even that notification was incomplete. On February 2, 2007, the Office of the U.S. Trade Representative requested WTO dispute settlement consultations, the precursor to convening a dispute settlement panel, with China concerning certain prohibited subsidies.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Please Note: Any person(s) and/or organization(s) wishing to submit for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, http://democrats.waysandmeans.house.gov, select "110th Congress" from the menu entitled, "Committee Hearings" (http://democrats.waysandmeans.house.gov/Hearings.asp?congress=18). Select the hearing for which you would like to submit, and click on the link entitled, "Click here to provide a submission for the record." Once you have followed the online instructions, completing all informational forms and clicking "submit" on the final page, an email will be sent to the address which you supply confirming your interest in providing a submission for the record. You MUST REPLY to the email and ATTACH your submission as a Word or WordPerfect document, in compliance with the formatting requirements listed below, by close of business **Thursday, March 29, 2007**. Finally, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office Buildings. For questions, or if you encounter technical problems, please call (202) 225–1721.

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1. All submissions and supplementary materials must be provided in Word or WordPerfect format and MUST NOT exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. All submissions must include a list of all clients, persons, and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone and fax numbers of each witness.

Note: All Committee advisories and news releases are available on the World Wide Web at http://democrats.waysandmeans.house.gov.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202–225–1721 or 202–226–3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman LEVIN. Mr. Herger and I understand there may be votes in about 10, 15 minutes, so let's try to do this.

We'll give our opening statements and then see. If possible, our distinguished colleague from Indiana can get his statement in, and then we'll recess and come back.

I want to make a few opening remarks, because I do think it's important that there be some background to this hearing on why I think, and why many others do, that action is long overdue.

The first point I would make, it's there, it's unassailable, relates to the trading relationship with China and our relationship, how unbalanced it is, and I think unsustainable.

One only has to look at the trade deficit figures.

In 2006, our trade deficit in goods was more than $232 billion, a 177 percent increase since 2000, and just look at the trade surplus figures China has worldwide. The first two months, the last two months, 39.7 billion.

So, I think that's point number one.

I think secondly that the legislation that has been introduced by Mr. Davis and Mr. English is one of the steps that can help bring about a more balanced trade relationship and more balanced rules of competition.

Thirdly, about the application of countervailing duty (CVD) law to nonmarket economies.

The Department of Commerce hasn't applied this for more than 20 years, and I know there's been a difference of opinion as to its application, and actually, I remember somewhat vaguely that we in Congress tried to change that on several occasions during the last 20 years.

Now, the Department of Commerce is saying that it will look into this issue, and yet the application of CVD is being challenged in the courts by China.

So, it seems to me this point is that Congress really needs to make it clear.

The next point I would make, I think it's unassailable, the extent of the subsidies of China: textile industry, steel industry, petrochemical industry, high-tech industry, forestry, machinery, copper, non-ferrous metals—on and on.

This list might be even longer if China had complied with its World Trade Organization (WTO) obligations.

It committed when it acceded to the WTO, and we debated that issue very much right here. It agreed to provide a subsidies report to the WTO in 2002 and it failed to do so 2003, 2004, 2005, and then finally in April of 2006, it provided a report, incomplete.

The next point I want to make, we should remember when we crafted Permanent Normal Trade Relations (PNTR), we asked for an annual review of China's obligations of its meeting its commitments within the WTO, and really, it failed to make that a meaningful annual review, and I do fault the Administration for failing to press China to do so.

The next point. When China acceded to the WTO, it agreed to eliminate all of its prohibited subsidies—those are export subsidies and import substitution subsidies—and yet the failure of China to submit its reports doesn't explain the inaction for all these years by the Administration to use these WTO mechanisms.

So, a case has been brought, I think it's long overdue.

So, we're going to hear from Mr. Visclosky, I think talking mostly about the steel industry.

Also, I think we're going to need to consider the semiconductor industry.

I have in my statement, which I think you may have a copy of, an example of how China has been subsidizing in that case the semiconductor industry of its country.

[The information follows: PENDING]

Chairman LEVIN. So, this bill really merits our Subcommittee's serious attention, and I appreciate, Mr. Davis and Mr. English, your introducing it, and your hard work on it.

This bill doesn't seek to, in quotes, "bash" a trading partner, but really, to try to make sure that the same rules apply to them as they do to everybody else, some balanced rules that provide for effective competition, and I emphasize that, balanced rules that bring about effective competition.

We'll perhaps discuss today or later on the provision in the bill for the role of Congress, and I simply urge there be serious consideration of it. It's not an effort to micromanage, it's an effort to make sure that Congress in this vital and other vital areas has a role.

So, I look forward with my colleagues to the testimony, and now I yield to the Ranking Member, Mr. Herger, for his opening remarks.

Mr. HERGER. Thank you, Chairman Levin.

Before remarking on H.R. 1229 specifically, let me first recall a hearing this Subcommittee held on China last month.

Witnesses and Members at that meeting, me among them, stressed the importance of U.S. trade with China. Specifically, I urged that we look at our economy as a whole and balancing interests of import-sensitive industries with the interests of U.S. industries that need imports to stay competitive.

At the same time, I noted my great displeasure with China's slow pace of reform with respect to ending unfair subsidies.

I urged the USTR to increase pressure and I was delighted to learn earlier this week that China has agreed to terminate a Central Bank subsidy program that gave large Chinese exporters discounted loans.

This was one of the subsidies captured in the WTO dispute settlement, preceding USTR has recently begun, but we can still do more, and that is why we are here today.

The bill we are discussing this afternoon, H.R. 1229, would apply countervailing duties to nonmarket economies. The prospect of countervailing duties will further increase pressure on all nonmarket economies, including China, to cease providing unfair subsidies to their domestic industries.

For this reason, I very much want to support this bill.

At the same time, however, we must also pay attention to what I referred to earlier as the balance. We cannot lose sight of the legitimate needs of U.S. manufacturers here on our own soil, a community that depends on foreign imports of inputs to compete with foreign firms and to keep the prices of consumer products down, which in turn increases our purchasing power and results in real income for American workers and families.

Further, our response to nonmarket economy subsidies must be in accordance with the U.S. law and our international obligations, particularly if we expect our trading partners to do the same.

Maintaining free and fair trade with nonmarket economies requires painting in small, deliberate strokes, not broad brushes.

There are three aspects of H.R. 1229 that, in my view, may be too broad.

First, the proposed legislation makes no mention of the possibility that domestic subsidies may be double counted when nonmarket economy countervailing duty cases are brought in conjunction with anti-dumping cases.

As the General Accounting Office has concluded, we need to provide the Department of Commerce with the authority to identify and correct instances of such double counting so that imports are not unfairly taxed. Without such explicit authority, Commerce has no means to address a known inequity in the process.

Second, Commerce uses data from within the subsidizing country to measure the benefit of unfair subsidies using third country data only if data from the subsidizing country is unreliable.

Contrary to these rules, H.R. 1229 creates an irrefutable presumption that data from within China is unreliable and inappropriately requires Commerce to use benchmarks from outside of China.

We don't want to hand China an easy opportunity to sue us in the WTO.

Third, H.R. 1229 requires that Congress consider a privileged approval resolution before Commerce is able to graduate a country from nonmarket to market economy status.

While I agree that congressional consultation during the graduation process is important, the procedure that H.R. 1229 proposes is cumbersome and unusual, given Commerce's technical expertise in this complicated field.

I look forward to discussion on these issues this afternoon, and am eager to work together to ensure that H.R. 1229 accomplishes the goal of free and fair trade with nonmarket economies.

As we move forward, though, it is critical that we maintain our focus on the U.S. economy as a whole and balance the interests of U.S. industries that compete against imports with the interests of those that need them to remain competitive.

Thank you.

Chairman LEVIN. Thank you very much.

Mr. Davis and Mr. English, if you would just briefly comment, if you like, and then Mr. Visclosky, and I think we can wrap this up and leave with. We've timed it three minutes to vote when there's sunshine outside.

Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman.

I will be brief, given Mr. Visclosky's time and the fact that we have a vote on.

I'll simply make two quick observations.

The first one, we're having an ongoing conversation and debate about how we build a consensus around trade in this economy, and Mr. Levin has been such a thoughtful, eloquent part of that debate.

It strikes me that it is impossible to build any consensus around trade unless we have a strong commitment to enforcement. That is what our consumers expect, it's what our producers expect, and frankly, it's what this institution expects.

That's all the core of this bill tries to do, to strengthen our commitment to enforcement to say that if rules apply to one set of countries, they need apply to another, and it leads to the second point that I want to make, and the last point that I want to make.

Every now and then, I'll pick up my editorial page and I'll read the Wall Street Journal or some other entity, and they will say that this kind of bill or this kind of measure is protectionist, and they'll say that all the steel industry wants is extra protections.

Let me just briefly describe protectionism to you:

> It's $1.67 billion worth of State financing for renovations at paper mills.
>
> It is $22.5 million worth of grants going to industries for capacity expansions.
>
> $7.25 billion going to fund bargain rate subsidized loans to State-owned steel enterprises.

The practitioners of what I've just described—not the United States Government, but the Chinese government. That's protectionism. All we're trying to do is to give us a reasonable, simple tool to address it and to stop it.

I'll yield back, Mr. Chairman.

Chairman LEVIN. Thank you for your eloquence.

Mr. English.

Mr. ENGLISH. Mr. Chairman, I would like to first of all thank Mr. Davis for leading on this legislation this year, and I would like to thank you for your prompt response in moving forward.

My hope, and I hope this dovetails into what Mr. Davis just said, which I fully support, that we can examine this issue objectively without any attempt to put it into political context, that we need to get into the details and recognize why this is good trade policy, to strengthen our trade laws, why it's broadly beneficial to the consensus we need to build on trade policy, and why it's helpful not just to specific industries, but to the overall performance of our economy.

I would simply say that last year, in the last Congress, because of what was going on on trade policy, our attempt to move similar legislation was not successful, but this year, on the details, I think we have an opportunity to go in with a clean slate and to consider the merits of this issue and see if we can give domestic producers and the Administration the tool that they need to confront some of the trade practices that have been eroding our manufacturing base.

I want to salute you particularly, Mr. Chairman, for being willing to be a leader on this, and I thank you for the opportunity to participate.

Chairman LEVIN. Thank you very much, Mr. English.

Mr. Visclosky, we welcome you as a distinguished activist colleague, and as chair of the caucus, of the Steel Caucus, and we have your bipartisan letter signed by 32 Members. So, take over.

Mr. VISCLOSKY. Mr. Chairman, thank you very much.

As I understand, my entire testimony will also be entered into the record?

Chairman LEVIN. It will be.

STATEMENT OF THE HONORABLE PETER J. VISCLOSKY, REPRESENTATIVE IN CONGRESS FROM THE STATE OF INDIANA

Mr. VISCLOSKY. Over and above the bipartisan letter signed by 32 members of the Steel Caucus, of which Mr. English is vice chair, we would ask that two additional addenda be added for the record, and that's two sheets detailing the 45 steel companies that entered into bankruptcy between the years 1997 and 2004.

Chairman LEVIN. It's so ordered. Thank you.

[The information follows: PENDING]

Mr. VISCLOSKY. I would thank you, Mr. Mr. Herger, and the Members of the Subcommittee for, one, holding a hearing on this very important issue, and secondly, for allowing me to testify, to express my strong support for H.R. 1229, the Nonmarket Economy Trade Remedy Act of 2007, and to thank my colleague, Mr. Davis, for his leadership, as well as Mr. English, as the lead co-sponsor.

I firmly believe that while H.R. 1229 will provide U.S. manufacturers with a crucial line of defense against illegally subsidized imports, I am also here to encourage your Subcommittee to look beyond countervailing duties, to the issue, among others, of foreign currency manipulation, in order to address fully the problems we face today.

Since 2000, the year China was granted permanent normal trade relations, the good-paying jobs of over 3 million American industrial workers have disappeared.

Over that same period of time, 23 percent of the domestic steel employment has been eliminated.

Since 1997, at the beginning of China's production explosion of the last ten years, 45 steel companies have gone into bankruptcy.

These are statistics. On the front page of the business section of the Washington Post today, there are details about foreclosures in those areas hardest hit.

I would note that the States of Michigan, Ohio, and Indiana are highlighted as areas with the greatest rate of sub prime loan foreclosures. They also suffer from the high unemployment rates. This is a human tragedy that has been allowed to occur.

From my perspective, as our jobs are being shipped overseas to China, the Chinese have enchanted this Administration with dialogue, just as the sirens tempted Ulysses with their song. We are defenseless as long as we are under their spell.

What I would like to emphasize is the word dialogue.

Mr. HERGER. alluded to the hearing that was held last month by your Subcommittee on February 17th.

That day, Timothy P. Stafford, assistant U.S. trade representative for China, testified. I am going to just read two sentences of his testimony, but listen carefully:

"While we have filed this WTO case, we continue to engage in dialogue with the Chinese on their use of subsidies.

These discussions are happening both at the sector specific level—for example, a recently created steel dialogue under the Joint Commission on Commerce and Trade (JCCT) is enabling a conversation among governments and industries of both sides as well as inc connection with our broader economic dialogues, including the strategic economic dialogue."

The guy mentioned dialogue four times in two sentences, alluded to a conversation and discussion.

In the meantime, I reference Members' attention to the chart that I have provided.

I am concerned about the abject lack of urgency the Administration attaches to this problem.

Mr. English was current and present and chairing the Steel Caucus last June when we had a hearing, and Mr. Jaime Estrada, deputy assistant secretary for manufacturing for the United States Department of Commerce, testified.

When Mr. English, I, and others were complaining about the lack of enforcement and protection for steel, Mr. Estrada had the audacity to say, "Well, we have countervailing duties," and when asked by the caucus, do they apply China, and this was a China steel specific hearing, he said, "Well, no." Who is the fool here?

Look at the chart. On March 24, 2005, the Administration launched their steel dialogue.

Steel exports by metric tons in January of 2006 were 312,000 tons. By March, we had our first steel dialogue.

By June of 2006, we had the caucus hearing and the dialogue was referenced again.

In July of 2006, when imports went up from 371,000 tons to 526,000 tons, perhaps the Administration talked to China. Perhaps when exports went up again to the United States in September of 2006, the Administration chatted with China.

We did have a second dialogue with China in October of last year, and imports again increased to the United States. They've gone up 65 percent in the last 12 months.

Fortunately, from my perspective, no further dialogues are scheduled. As we meet today, they're killing us, these dialogues, but there was a consultation on February 12th.

I would implore the Committee to give careful consideration to the legislation that has been introduced by Mr. Davis and Mr. English and also ask that you seriously consider other options so that we can ensure it is a fair, level playing field for American workers.

[The prepared statement of Mr. Visclosky follows:]

Prepared Statement of The Honorable Pete Visclosky, Representative in Congress from the State of Indiana and Chairman of the Congressional Steel Caucus

Thank you Chairman Levin, Ranking Member Herger, and Members of the Subcommittee for the opportunity to testify before you with respect to the first critical step in what I hope will be comprehensive trade law reform. H.R. 1229, the Nonmarket Economy Trade Remedy Act of 2007, is a good first step, but we need to do more. The American steel industry faces unprecedented challenges from countries like China, which compete unfairly in the global marketplace. Too many good-paying American manufacturing jobs have been shipped overseas, and the steelworkers I represent need comprehensive legislation to address the growing threat posed by China.

My appearance here today as Chairman of the Congressional Steel Caucus, a bipartisan group of 107 Members of Congress, should underscore the broad-based support for fair-trade measures like H.R. 1229 in the House. Our colleague, Representative Phil English, who is the Vice-Chairman of the Steel Caucus and a Ways and Means Committee Member, would attest to this as well. But while I firmly believe that H.R. 1229 will provide U.S. manufacturers with a crucial line of defense against illegally subsidized imports, I am also here to encourage this Subcommittee to look beyond Countervailing Duties, to the issue of foreign currency manipulation, in order to address the full problem we are facing today. My message, simply put, is that if we are to maintain a manufacturing base in the United States, we **must** have zero tolerance for unfair and illegal trade. We must fight back on many fronts, from China's subsidization activities to their continued manipulation of their currency. The imminent challenges facing the steel industry cannot wait to be addressed.

As the Representative for the Indiana's First Congressional District, I am proud of the contribution my own district makes to the nation's economy in the production of steel. In 2005, 17,588 people worked in steel-related jobs in Lake and Porter Counties. In perspective, those steelworkers make up over 75 percent of Indiana's steel workforce, and over 11 percent nationwide.

I am very encouraged by the legislation introduced by Rep. Artur Davis and Rep. English. In my opinion, H.R. 1229 is one of the most important proposals for the steel industry that has received serious consideration in recent years. That is why, earlier this week, I submitted a letter to the Chairman and Ranking Member of the full Committee, Rep. Rangel and Rep. McCrery, a copy of which I will submit with my testimony today. This letter expressed the support of 32 Members of the Steel Caucus for the prompt consideration of H.R. 1229.

As this Subcommittee knows, H.R. 1229 would improve the tools available to U.S. manufacturers in order to defend against illegal imports. The most important of these tools is the application of Countervailing Duties (CVD) to Nonmarket Economies. CVD law provides for the assessment of import duties in an amount equivalent to the amount of the subsidy received on that imported product. When we in the steel community talk about nonmarket economies, we usually talk about China. As this Subcommittee was made aware during its February 15, 2007, hearing on trade with China, there are very clear reasons for this attention.

Over the last ten years, Chinese crude steel production more than quadrupled, growing from an estimated 100 million Metric Tons (MT) in 1996 to approximately 420 million MT in 2006. In other words, China has built the equivalent of three entire American steel industries, in terms of annual steel production, in just ten years. China's share of world steel production, which was estimated to be one-eighth in 1996, mushroomed to over one-third in 2006. This industrial growth is unprecedented in history.

It is no coincidence that these increases in steel production have come during periods of immense government subsidization of China's steel industry. This issue is perhaps the most crucial problem facing the global steel industry, as well as many other industries, today. Reports, some from the Chinese government itself, detail preferential loans, debt forgiveness, raw material market subsidies, energy subsidies, and direct government ownership of steel companies.

As you know, just last year, China finally submitted its subsidies notification to the World Trade Organization (WTO)—four years late and certainly lacking in forthrightness with regard to disclosure of subsidies. Still, the report identified over 70 subsidy programs, which, coupled with lax labor and environmental standards and the manipulation of their currency, amount to warfare on American steel workers.

How can our steel industry respond to these attacks? The President rejected the recommendations of the International Trade Commission (ITC) in all four petitions that have come to him under the China-specific Section 421 safeguard since the year 2000. Countervailing Duties, a trade remedy proven to be effective against the subsidization of products such as steel, have been rendered useless against China by our own Department of Commerce in repeated cases over the last 20 years. However, the world has changed a lot since the 1984 "Georgetown Steel" case, and our trade policies should reflect that. For example, China's accession to the WTO in 2001 required the adoption of the WTO Agreement on Subsidies and Countervailing

Measures, as well as the adoption of more specific definitions of subsidies in the WTO. Obviously, as evidenced by the four-year delay on their WTO subsidies report, these obligations have not been taken seriously by China.

What is so discouraging to me is how long it has taken for the Executive Branch to take action on these blatant violations. As our jobs are being shipped overseas, the Chinese have enchanted the Administration with "dialogue," just as the Sirens tempted Ulysses with their song. Like Ulysses, we are defenseless against Chinese imports unless we take real, concrete actions to stop our ship from crashing against the rocks. While I welcome the recently filed WTO petition by the U.S. Trade Representative and the potential investigation by the Department of Commerce into CVDs on coated paper from China, I am alarmed by the lack of urgency to their efforts.

Of course, this lack of concern has resulted in winners and losers, so let's talk about that. Since 2000, the year China was granted permanent normal trade relations, the good-paying jobs of over 3 million American industrial workers have disappeared. Over that same time period, 23 percent of the domestic steel employment has been eliminated. Since 1997, at the beginning of China's production explosion of the last ten years, 45 steel companies have gone into bankruptcy, as this chart, which I submit for your reference, details.

Indiana has been hit particularly hard by this recent downswing. While nearly 24,000 Hoosiers work in steel-related jobs today, this is just a fraction of the jobs held not that long ago. Indiana has lost about one out of every four steel mill jobs in the state since President Bush took office, with heart-breaking consequences. Each lost job has meant lost wages, lost health care, and lost retirement benefits for a family. Communities are losing their residents as people must move on. It is clear that American workers have absorbed the brunt of the Administration's trade agenda.

While H.R. 1229's CVD provisions are crucial, several other provisions of this measure will prove useful in improving the Congress' ability to influence trade policy. The measure would create a new mechanism in which Congressional approval would be required to implement a decision by Commerce to "graduate" a country from nonmarket to market economy status. This is important for several reasons. Under existing law, the executive branch has sole authority to determine when a nonmarket economy country meets the criteria of a market economy under U.S. antidumping duty law. I am concerned by the pressure China is already applying on the President to prematurely graduate them to market economy status, both for symbolic value and to reduce the margins they are subject to on antidumping orders as a non-market economy. This pressure could become even greater if countervailing duties are applied upon passage of H.R. 1229.

For an example of this, we need only to look back to 2002, when President Bush graduated Russia from nonmarket to market economy status not long after the September 11 attacks. Much of Russia's economy was still centrally controlled, but the President granted this status anyway. We cannot allow American workers to be sold out for political advantage. By adding an up-or-down vote in Congress, this process would be no different than the "Fast-Track" authority that the President already has. This Administration's failure to address the growing threat and manipulation of the marketplace by the Chinese is yet another reason why comprehensive trade legislation is needed.

Further, H.R. 1229 would direct the International Trade Commission (ITC) to conduct an annual study of Chinese government intervention to promote investment, employment, and exports. The ITC would be directed to submit its findings to Congress every year through 2017. This information will be vital to the Congress as we continue to improve our defenses against illegally subsidized imports.

My testimony would not be complete without addressing another major issue that I have touched on already regarding the problems that China poses to our manufacturing base. This issue is currency manipulation. I am a cosponsor of H.R. 782, the Ryan/Hunter Fair Currency Act of 2007, which would help to eliminate the unfair advantage that Chinese producers have gained due to their government's daily manipulation of their currency. This problem has grown to be so massive that economists, such as Dr. Peter Morici of the University of Maryland, believe the Yuan could be undervalued by 30 to 50 percent. While the Steel Caucus has endorsed the provisions of H.R. 1229, the Nonmarket Economy Trade Remedy Act of 2007, I must recommend that this Subcommittee work to expand this measure to address the problem of currency manipulation, which acts as a weight around the neck of every American manufacturer.

I am impressed by the foresight shown by today's steel companies in America. They have seen the challenges on the horizon, and they have continued to use their profitability to improve efficiencies and their product mix as they prepare for difficult times ahead. They are focusing on high-value products. They are making the investments necessary to remain competitive.

However, American steelmakers continue to lose their market to Chinese companies that, despite having higher energy and raw material costs per ton of steel and lower worker productivity than U.S. steel producers, are somehow able to offer cheaper steel. How is this possible? Subsidies and currency manipulation make up the difference. These companies cannot compete with our steel industry on a level playing field.

I know we have the most efficient, productive, and skilled steel industry in the world. But even with that edge, our producers cannot prevail in a contest where only they have to play by the rules. If our companies cannot count on a level playing field, then U.S. manufacturing has no long-term future.

Now is the time to strengthen our trade laws. We are too late to save the 45 bankrupt mills I mentioned. However, if we can get out ahead of this next major crisis with sound policy, including H.R. 1229 and currency manipulation reform, then we will have done our best for the workers who are counting on us. Thank you again for the opportunity to appear before this Subcommittee today.

Chairman LEVIN. Thank you, very, very much, Mr. Visclosky, for your dedicated efforts.

We stand in recess.

How many votes do we have? Two? Two votes.

Well, two votes means 15 minutes, hopefully not more.

Mr. VISCLOSKY. Mr. Chairman, thank you very much.

Chairman LEVIN. Thank you very much.

[Recess.]

Chairman LEVIN. My apology. It was an unexpected series of events.

The Appropriations Committee was trying to finish the supplemental, and so we held open the vote for, it must have been 30 minutes, because they needed to finish and get the bill out today so it could be brought up next week. As you know, it has some important provisions in it.

I think ordinarily, we would not have waited for the Appropriations Committee to finish, but it was decided to do so.

So, my apology. I said semi-humorously I wasn't sure if it would be 15 or 20 minutes, and it was an hour.

Let me just check.

[Pause.]

Chairman LEVIN. All right. Let's begin.

Again, we'll make sure that all of the information, all the testimony is well distributed.

Let me say, some have asked is there a scheduled date for markup on this bill, and the answer is there isn't, except there's a strong desire to move it.

So, there will be further opportunity for the full Committee to consider this, and I urge everybody to make sure that there's the fullest interchange between yourselves and Members of this Committee, because I do think that it's likely that there will be action in the foreseeable future.

All right.

Kevin, welcome.

So, we'll continue with David Spooner, who is assistant secretary for import administration, International Trade Administration (ITA), Department of Commerce.

Again, my apology to you, as well as to the others.

Proceed, if you would.

Mr. BRADY. Mr. Chairman, if I may interrupt for just one moment.

Chairman LEVIN. Absolutely.

Mr. BRADY. I apologize. The delay in those last votes has caused me to head to the airport.

Could I have unanimous consent to introduce into the record a letter from General Motors dealing with the countervailing duty law in our Committee's review of this legislation?

Chairman LEVIN. Absolutely.

Mr. BRADY. Thank you.

Chairman LEVIN. It's so entered.

[The information follows:]

GM

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Via Email & Post

January 12, 2007

Ms. Susan H. Kuhbach
Senior Office Director for Import Administration
U.S. Department of Commerce
14th Street and Constitution Avenue, NW
Room 1870
Washington, DC 20230

Subject: Application of the Countervailing Duty Law to Imports from the People's Republic of China

Dear Ms. Kuhbach:

On behalf of General Motors Corporation, I would like to respond to the Department of Commerce's request for public comments on applying U.S. countervailing duty law (to offset foreign subsidies) to imports from China.

First, I would like to stress that it is clear that unfair pricing and government subsidies of exported goods may distort the free flow of goods and adversely affect the competitiveness of U.S. products. Accordingly, we support U.S. policies, including robust anti-dumping and countervailing duty laws, that provide U.S. firms reasonable recourse against the unfair trade practices of foreign companies and countries.

At the same time, it is important to recognize that overuse of such tools can also distort trade flows and hurt the competitiveness of industries that consume foreign goods and materials. Specifically, the imposition of punitive duties on imports can lead to higher prices and reduced availability of critical parts and materials. It is precisely because of these potentially damaging impacts that the Department and the International Trade Commission are obligated to conduct "sunset reviews" every five years to determine whether it is necessary that anti-dumping and countervailing duties remain in place.

Given these considerations, General Motors takes the position that the use of anti-dumping and countervailing duty law and the methodologies used to identify and address unfair trading practices must be fair and balanced, and that the methodologies used to establish

Ms. Susan Kuhbach
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unfair trade practices should not unduly handicap imports that are fairly traded or do not result in material injury to domestic producers.

With regard to the specific issue of non-market economies, both case law and the Department of Commerce's current practice have recognized the difficulty of accurately measuring the amount of subsidies provided in non-market economies. However, any advantage gained by such economies because of the reluctance of the US to pursue subsidy cases has clearly been offset by the disadvantage that non-market economies experience in anti-dumping cases. Since World Trade Organization rules allow the use of factors of production analysis as a proxy for prices in non-market economies, designation as a non-market economy represents a significant penalty in anti-dumping proceedings, particularly in the US where factors of production analysis is routinely used.

Given this situation, we believe that industries should be treated consistently in both countervailing duty and anti-dumping proceedings. If the Department of Commerce establishes that an industry in a non-market economy is developed enough to be considered as if it were part of a market economy (and, therefore, subject to countervailing duty action), then we believe that industry should also be treated as a market economy for the purposes of any anti-dumping investigations.

We appreciate the opportunity to offer our comments for this review.

Sincerely,

Mustafa Mohatarem

Chairman LEVIN. Mr. Spooner.

STATEMENT OF THE HONORABLE DAVID M. SPOONER, ASSISTANT SECRETARY FOR IMPORT ADMINISTRATION, INTERNATIONAL TRADE ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE

Mr. SPOONER. Thank you, Chairman Levin and Congressman Brady and other Members of the Subcommittee, for inviting me to discuss the Nonmarket Economy Trade Remedy Act of 2007 introduced by Representatives Davis and English.

I appreciate the opportunity to share with you the Department of Commerce's views on this bill, particularly as it relates to the application of the countervailing duty law to China and other nonmarket economy countries.

China's remarkable economic growth in recent years makes it one of the most important engines of the world economy outside of the United States. In trade terms, China represents one of the fastest-growing markets for U.S. goods and services.

Our exports to China, which for the most part are high-value-added products, totaled $55 billion in 2006, growing at a rate of

32 percent from the previous year. That makes China our fourth largest export market.

To help ensure continued and increased growth of U.S. exports to China, the United States is working proactively to identify and seek the removal of barriers to U.S. exports.

Unfair subsidies inside China distort trade conditions for U.S. producers and exporters. The Chinese press is rife with examples of subsidies given to various sectors.

China clearly employs subsidies. The question is, what domestic and international strictures we can use to discipline them.

At the Commerce Department, we are charged with the enforcement of U.S. trade remedy laws, including our domestic anti-subsidy law, the countervailing duty law.

Let's make no mistake about it, subsidies exist in China and are distorting the playing field. There is no legal bar to Commerce's application of the CVD law to nonmarket economies, including China, and we will do so if presented with the appropriate facts.

As you know, countervailing a nonmarket economy poses unique challenges, such as calculating benchmarks for subsidy programs.

Moreover, applying U.S. CVD law to countries like China that are classified as nonmarket economies for anti-dumping purposes raises complex issues of policy and methodology which could have implications for other aspects of Commerce's trade remedies practice.

Nevertheless, current law allows us to countervail China. Indeed, as you know, Mr. Chairman, we are now conducting a countervailing duty investigation of coded free sheet paper, glossy paper, from China, that dates from last fall.

The petition in that investigation was filed by NewPage Corporation, which testified before I believe this Subcommittee in February.

We will be announcing our preliminary determination in the glossy paper investigation by April 2nd, so it would be inappropriate for me to comment upon the specific merits of that investigation at this time.

For more than 20 years, indeed throughout four Administrations, Commerce has maintained a policy of not applying our CVD law to countries that we have classified as nonmarket economies for anti-dumping purposes.

The basis for this policy was the 1984 Georgetown Steel decision in which the court affirmed that Commerce has the discretion to decide whether or not to apply the CVD law to nonmarket economies (NME).

Since then, Commerce has had a practice of not applying the CVD law to NME countries, including China, and the anti-dumping law has been a commonly used instrument to address unfair trade practices on the part of Chinese producers and exporters.

Our decision to conduct the CVD investigation in the glossy paper case in no way reverses our decision, reaffirmed just last August, to treat China as a nonmarket economy under the anti-dumping law.

The glossy paper investigation represents the first CVD petition for China received by Commerce since 1991. The present investigation, therefore, provides us with an opportunity to review our longstanding policy of not applying the anti-subsidy law to nonmarket economies.

Given the complex legal and policy issues involved in our upcoming decision on December 15th, we requested public comment on the issue. We received over 50 responses, including comments from Senators, House Members, National Association of Manufacturers (NAM), and other industry groups.

The majority of the commenters cited concerns about the growing problem of Chinese government subsidies and the adverse impact that they have on U.S. producers and workers.

As such, the majority of commenters encourage Commerce to apply the CVD law to imports from China.

We are in the process of carefully reviewing all these submissions and other relevant information on the record before making our preliminary determination in the glossy paper case.

We are committed to identifying and addressing unfair subsidies in all countries, including China. That is a top priority for us.

We will not hesitate to use the tools at our disposal to discipline China's use of unfair subsidies.

Make no mistake about it. If we can formulate a methodology for countervailing nonmarket economies, we will not give any country a free pass when it comes to illegal and distortive subsidies.

Commerce has always maintained, and we believe the courts have agreed with us, that we have the authority to apply the CVD law to NME countries. However, if Congress would like to affirm Commerce's authority, as the House did in 2005, and as H.R. 1229 does, we would welcome this opportunity to work with you, Mr. Chairman, and other Members of the Committee.

Thank you for giving me this opportunity to testify before you on this topic today.

[The prepared statement of Mr. Spooner follows:]

David M. Spooner
Assistant Secretary of Commerce for Import Administration
March 15, 2007
House Ways and Means Committee, Subcommittee on Trade

Thank you Chairman Levin, Ranking Member Herger, and Members of the Subcommittee for inviting me to discuss the "Nonmarket Economy Trade Remedy Act of 2007" (H.R. 1229), introduced by Representatives Davis and English. I appreciate the opportunity to share with you the Department of Commerce's views on this bill, particularly as it relates to the application of the countervailing duty (CVD) law to China and other non-market economy (NME) countries.

China's remarkable economic growth in recent years makes it one of the most important engines of the world economy outside of the United States. In trade terms, China is now the United States' third largest goods trading partner. China represents one of the fastest-growing markets for U.S. goods and services. Our exports to China, which for the most part are high value-added products, totaled $55 billion in 2006, growing at a rate of 32 percent from the previous year. That makes China our fourth largest export market. At the same time, China is our second largest source of imports. U.S. goods imports from China totaled $288 billion in 2006, an 18 percent increase over 2005.

To help ensure continued and increased growth of U.S. exports to China, the United States is working proactively to identify and seek removal of barriers to U.S. exports. Unfair subsidies from the central, provincial, and local governments to Chinese companies distort trade conditions for U.S. producers, both here in the U.S. market and abroad. These subsidies are available across manufacturing sectors, so they can provide an unfair advantage to China's exports of a wide range of products to the United States.

They can also harm U.S. producers hoping to export successfully to China or compete with Chinese exports to third country markets. The Chinese press is rife with examples of subsidies given to various sectors from agricultural products to steel. China clearly employs subsidies; the question is what domestic and international strictures we can use to discipline them.

At the Department of Commerce, we are charged with the enforcement of U.S. trade remedy laws. Before talking about our work at the Import Administration, I want to discuss the work of the Office of the U.S. Trade Representative (USTR), which recently has taken steps to discipline Chinese subsidies that appear to be prohibited under the rules of the World Trade Organization (WTO).

In April 2006, more than four years after its accession to the organization, China submitted its first subsidies notification to the WTO, an annual requirement for all WTO members. China identified over 70 subsidy programs, but the notification was incomplete. Furthermore, China did not indicate any intent to withdraw or reform several notified programs that appeared to be prohibited. On February 2, 2007, USTR requested WTO dispute settlement consultations with China concerning these and other Chinese subsidy programs that appear to violate WTO rules. Six of the challenged subsidy programs appear to be export subsidies, granted on the condition that the recipients meet certain export performance criteria. The remaining three programs appear to be import substitution subsidies, conditioning the grant of subsidies on the recipient's purchase of domestic goods over imported goods. Both export subsidies and import substitution subsidies are prohibited under the WTO Agreement on Subsidies and Countervailing Measures. The United States and China have not yet held WTO consultations on this matter, but I would like to note that last week China unilaterally rescinded one of the alleged export subsidy programs.

That is the role of USTR – to enforce U.S. rights at the WTO. We at the Commerce Department enforce our domestic anti-subsidy law, the countervailing duty law.

Let's make no mistake about it: Subsidies exist in China and are distorting the playing field. There is no legal bar to Commerce's application of the CVD law to non-market economies, including China, and we will do so, as long as appropriate circumstances warrant such application. As you know, countervailing a non-market economy poses unique challenges, such as calculating benchmarks for subsidy programs. Moreover, applying U.S. countervailing duty law to countries like China that are classified as non-market economies for antidumping purposes raises complex issues of policy and methodology, which could have implications for other aspects of Commerce's trade remedies practice. Nevertheless, current law allows us to countervail China.

Indeed, we are now conducting a countervailing duty investigation of coated free sheet paper (glossy paper) from China that dates from last October. The petition in that investigation was filed by NewPage Corporation, which testified before this Subcommittee in February. We will be announcing our preliminary determination in the glossy paper investigation by April 2, so it would be inappropriate for me to comment upon the merits of that investigation at this time.

I would also note that the Government of China has challenged Commerce's initiation of the CVD glossy paper investigation at the U.S. Court of International Trade and has requested a preliminary injunction. The Court has not yet ruled on that request, although it did deny China's initial motion for a temporary restraining order that would have prevented Commerce's investigation from going forward.

For more than 20 years, throughout four Administrations, Commerce has maintained a policy of not applying our CVD law to countries that we have classified as non-market economies for antidumping purposes. The basis for this policy was the 1984 Georgetown Steel decision, in which the Court of Appeals for the Federal Circuit affirmed that the Department of Commerce has the discretion to decide whether to apply the countervailing duty law to non-market economy countries. In the circumstances presented by that case, Commerce reasoned that non-market economy firms were not independent, profit-driven allocators of resources and, therefore, could not take into account the impact of government subsidies when making pricing decisions. Since then, Commerce has had a practice of not applying the CVD law to NME countries, including China, and the antidumping law has been a commonly used instrument to address unfair trade practices on the part of Chinese producers and exporters. We currently have 61 antidumping orders against China. Since 2001, we have issued 31 antidumping orders against China, compared to the 24 orders put into place between 1993 and 2000. Our decision to conduct this countervailing duty investigation in no way reverses our decision, reaffirmed last August in the context of the antidumping investigation of imports of lined paper from China, to treat China as a non-market economy country under the antidumping law.

The glossy paper investigation represents the first China CVD petition received by Commerce since 1991, when we initiated investigations on lugnuts and ceiling fans. In both of those cases, Commerce ultimately did not find a basis for applying the CVD law to the industry in question, consistent with Georgetown Steel. The present investigation provides Commerce an opportunity to review its long-standing policy of not applying the CVD law to NMEs, such as China.

Given the complex legal and policy issues involved in our upcoming decision, on December 15, 2006, Commerce requested public comment on this issue. We received over 50 submissions in response to this request, including comments from a group of Senators, House members, the National Association of Manufacturers (NAM), and various other industry groups. The majority of the commenters cited concerns about the growing problem of Chinese government subsidies and the adverse impact they are having on U.S. producers, workers, and farmers. As such, the majority of commenters encouraged Commerce to begin applying the CVD law to imports from China. At the same time, Commerce also received comments from several U.S. consuming industries encouraging Commerce to maintain its current policy and not to apply the CVD law to non-market economies. Commerce is in the process of carefully reviewing all of these submissions and other relevant information on the record before making its preliminary determination in the glossy paper investigation.

We are committed to identifying and addressing trade-distortive and injurious subsidies from all countries, including those in China. That is a top priority for us. Import Administration will not hesitate to use the tools at our disposal to discipline China's use of unfair subsidies. Make no mistake about it; if we can formulate a methodology for countervailing non-market economies and are provided with the appropriate set of facts, we will not give any country a free pass when it comes to illegal and distortive subsidies.

Commerce has always maintained, and we believe the courts have agreed with us, that we have the statutory authority to apply the CVD law to NME countries. However, if Congress would like to affirm Commerce's authority, as proposed under Section 2 of H.R. 1229, we would welcome the opportunity to work with you, Mr. Chairman, and with this Committee. I should note that, because of the complexity of this issue, it is important for the language of any bill to be crafted with appropriate precision, not only to ensure consistency with our international trade obligations but also to avoid unintended consequences for existing provisions of U.S. countervailing duty law.

Thank you for giving me this opportunity to testify on this important topic today.

Chairman LEVIN. Thank you very much.

Let's proceed in this order.

I know Mr. Davis has another markup, so why don't you go first instead of me, and then, Mr. Herger, you'll go next, and then I'll come after you.

Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman.

Mr. Secretary, I apologize to you. I have a markup, literally in another Committee, so I'm trying to squeeze out some time before I have to go cast a few votes.

Let me, and I don't suspect I'll take the full 5 minutes, but let me focus on one aspect of your testimony.

You mentioned that one of the reasons that the Administration has not been so keen on applying countervailing duties is that there are remedies available on the dumping front. I think you said that in your testimony.

I wanted to challenge that premise.

Obviously, dumping is a problem in its own right, and there are remedies available to deal with dumping, but if I understand it correctly, subsidies are a different kind of problem, a different species of problem.

Among other things, subsidies violate the WTO standards. I don't think there's any dispute about that.

In addition to that, subsidies obviously cause market-distorting effects which are perhaps, in kind, they may play out in the same way that dumping does, but they are different.

So, explain to me again why it would be injurious to have this extra set of tools to use.

Mr. SPOONER. Thank you, Congressman Davis.

I actually agree, I think. I hope I didn't imply, I certainly didn't mean to imply that applying the CVD law to China would be unnecessary.

While it's true that we've been aggressive about applying the anti-dumping law to China—I think 25 percent of all cases now are on Chinese imports—you're right, the CVD law addresses an entirely different type of unfair trade practice.

The reason it has been, frankly, until now, when we have this ongoing investigation in the glossy paper case that we've—the reason it's taken until now to launch an investigation has, frankly, to a certain degree, been simply because we haven't had a petition until last fall.

Mr. DAVIS. Would countervailing duties or the possibility of applying countervailing duties itself be a bargaining chip for the United States in our dealings with China?

Mr. SPOONER. That's a good question, Congressman.

I hope I put this well.

We have to use all the tools in the toolbox. I mean, Congressman, Chairman Levin in his—I'm sorry, it was Mr. Visclosky, in his something, was essentially saying, I think, although I hesitate to paraphrase a Member, that we shouldn't only have dialogue, that we should enforce, as well.

Frankly, I agree with that. We should have ongoing dialogue, ongoing diplomacy with the Chinese, such as we do in the steel dialogue, but if we show a willingness to enforce our law as we should, I think that complements our dialogue.

Mr. DAVIS. Have you reviewed—I assume that you've reviewed the bill that Mr. English and I have introduced?

Mr. SPOONER. Yes, sir.

Mr. DAVIS. Do you agree with me that there's nothing in that bill that speaks to the currency devaluation issue?

Mr. SPOONER. Yes, sir.

Mr. DAVIS. Mr. Chairman, I will yield back.

Chairman LEVIN. Thank you so much for your hard work and your coming, and don't miss votes. That's why we held open the last vote for 45 minutes.

Mr. Herger, our Ranking Member.

Mr. HERGER. Thank you, Mr. Chairman.

Mr. Spooner, I believe that Commerce should consult with Congress prior to revoking a country's nonmarket economy status, but I believe that requiring an Act of Congress first is unprecedented.

Do you have plans to revoke China's nonmarket economy status in the next year, or even within the next five years; and what changes will you need to see in China in order to entertain doing so?

Mr. SPOONER. I can assure you, Congressman Herger, that I don't.

Indeed as you know, just last August, Commerce reaffirmed China's status as a nonmarket economy, and when we did so, we issued, I think it was an 84-page memorandum describing the reasons for our decision, and the memo is rife with ways in which China has yet to jump over the hurdle, so to speak, including the free flow of labor within China, distortions within China's banking sector, problems with the rule of law in China.

All those things, among others, would have to be rectified before we were to consider graduating China to market economy status.

Mr. HERGER. Thank you.

You mentioned in your testimony that it's important for any bill applying the CVD law to China to be crafted with appropriate precision, not only to ensure consistency with our international obligations, but also to avoid unintended consequences for existing provisions of U.S. CVD law.

Could you elaborate?

Mr. SPOONER. Thank you, Congressman Herger.

I think briefly, at least with respect to our domestic law, it's more USTR than Commerce that evaluates our WTO consistency, but I had two, perhaps, specific drafting questions, at least.

One was the way in which the portion of the bill which would require a congressional motion of approval or disapproval with market economy decisions.

Under law, we have to decide our cases under very certain rigid timelines and it's unclear from the bill whether or not that disapproval motion would make us miss our deadlines, so to speak.

I think another question we had was whether that provision amounts to—represents a desire on behalf of the drafters to take a second look at Commerce's analysis in market economy decisions or whether—I hope I put this well—it represents a desire to sort of put aside what Commerce is supposed to look at when we do market economy evaluations and have Congress consider other factors which aren't—which Commerce isn't supposed to look at.

Mr. HERGER. Could you please tell us the criteria that you use in determining whether to use information from a nonmarket economy in an anti-dumping investigation?

Do you routinely exercise your discretion to disregard such information and use surrogate data if that information is not adequate?

Mr. SPOONER. We do routinely do so, yes, sir.

Indeed, when we designate an economy to be a nonmarket economy, as we do with China, in every dumping case, we go outside of China and use surrogate country values.

Mr. HERGER. Thank you.

Thank you, Mr. Chairman.

Chairman LEVIN. Thank you very much, Mr. Herger, for your questions.

I want to really focus on where we go from here, but I must say, when you say in your testimony, you repeated it, Mr. Spooner, that the reason there hasn't been any action by Commerce is because no petition was filed, it's hard to expect that a petition be filed when there's a policy that the petition will be discarded.

So, I don't really think that is a convincing rationale. I think instead, there has been a policy decision, because it could be reversed without the need for a petition.

I think as the nonmarket economies grew in this world of ours, in this economic world, there was a need to revise the policy when you had the power. This is somewhat before your time.

So, I want to focus on the future, but I think it isn't wise to use what I think is kind of an irrational excuse for what I think was an increasingly irrational policy.

Secondly, let me just mention, on the—and we're going to work together on this, so I say that somewhat gently, but there's a lot of feeling about this, especially as China began to be a major, major competitor.

Let me just say a word about the congressional disapproval provision.

I hope we'll work with you on it. You answered Mr. Herger's salient question that—I don't know if you wanted to commit yourself for five years; I don't think anybody can do that. I think if one looks back at the history of how we handled the Soviet Union's position, I don't know that—and I haven't gone back over the papers, but my guess is that there were fairly elaborate documents talking about the hurdles that had to be jumped by the Soviet Union, or maybe that's not the correct terminology, the practices that had to be remedied before we could take that action, and yet the action was taken.

I would hope we could focus on the role of Congress on decisions of importance like this.

It does reflect, I think, a strong feeling that there has to be a major change in the role of Congress not to negotiate but to be sure that we are active, meaningful partners.

Let me just ask you then one last thing.

It relates to an issue that has been raised here, and the so-called double counting issue.

So, let me ask you whether you think that this is an issue regarding the application of CVDs and anti-dumping duties to a nonmarket economy and its methodology; do you see this as an issue?

Mr. SPOONER. Thank you, Mr. Chairman.

Frankly, as you know, the Government Accountability Office (GAO) report did a—I'm sorry—the GAO did a report two years ago on difficulties that Commerce might encounter in applying the CVD law, and they identified this double counting issue as something that might be an issue for Commerce. Frankly, I wouldn't go so far.

Whether or not we face double counting should we apply the CVD to China will be a very fact-intensive, case by case thing, and frankly, I think we will just have to see in the context of a specific case whether or not we face double counting, and then go to the next step of if so, how do we address it.

Of course, we would work closely with you to figure out how to do so.

Chairman LEVIN. Are you saying that there isn't any overall basic issue of double counting?

Mr. SPOONER. We just haven't seen it yet. We haven't——

Chairman LEVIN. As you've worked on these issues, you haven't seen it?

Mr. SPOONER. Yes, sir.

Chairman LEVIN. Okay, thank you.

Mr. SPOONER. Sure. I should say, sir, as we do our market economy decisions, I can promise you—I should have conveyed this to Congressman Herger—that we would consult closely with Congress, and particularly Members of this Committee.

Chairman LEVIN. All right.

So, as you leave, as I understand it, you say case by case, so do I correctly assume that you don't see a need for a specific provision in this bill on double counting?

Mr. SPOONER. We—Commerce I believe would prefer to wait until we had some hands-on experience should we apply the CVD law to China before we crafted the legislative fix, should we need one.

Chairman LEVIN. So, I think your answer is no?

Mr. SPOONER. Yes, sir.

Chairman LEVIN. Thank you. There's no need for such a provision.

All right. Mr. English, welcome. Glad you were able to rejoin us, after that long, long hiatus on the floor.

Mr. ENGLISH. I unfortunately did.

Mr. Spooner, thank you for your testimony.

I think I'm on the same wavelength as the Chairman on the issue of double counting.

If I could just revisit this, on the next panel, my understanding is that we're going to hear from a member of the Washington Trade Bar that cites a 2005 GAO report stating that Department of Commerce doesn't currently have the legal authority to devise a methodology for applying countervailing duty law to nonmarket economies, which takes into account the theoretical practice of double counting.

Is that an accurate characterization of the GAO and is it fair to say that is not Commerce's position?

Mr. SPOONER. Yes, sir, it's fair to say that that is not Commerce's position.

The GAO report, if I remember it correctly, stated that Commerce does not have the explicit statutory authority to apply the CVD to China, and it's been our longstanding claim that we have the implicit statutory authority to do so.

Indeed, the key portion of the statute, which is amended in Section 1(a) of H.R. 1229, refers to all countries, not just market economy countries.

Mr. ENGLISH. I guess that's probably, given the fact that you are pursuing the coated paper case now, probably about as far as we need to go on that, although do you feel that the language of the bill, as we've tried to craft it, gives you adequate authority to go forward with the coated paper case without interruption, bearing in mind, and I understand this may have been brought up while I was on the floor, but Mr. Davis was very careful, I think, to draft this legislation to not disrupt the current Commerce activities, and in fact, the retroactivity provision, which I understand is also criticized in some later testimony in the next panel, is intended simply to provide for continuity.

Is that your appreciation of the language?

Mr. SPOONER. For the most part, Congressman English, I think that's the case.

There's one provision of H.R. 1229 which may impact our practice, and I can't comment as to whether it would impact our glossy paper analysis.

Should we decide to countervail China, rather nonmarket economies, under current law, we can—our job is basically to figure out, to do the math, as—would be to do the math as best we can, and that might involve looking at benchmarks within China under appropriate circumstances, or it could involve looking outside China.

There's one portion of H.R. 1229 which would require Commerce to look outside China under all circumstances that we might want to work with the Committee on.

Otherwise, I think it would affirm our authority.

Mr. ENGLISH. Let me just say, Mr. Spooner, I'm delighted that you're here to testify.

I also want to express, since the Administration has been criticized at this hearing, in that there are some deep policy differences on the question of China trade, I for one am grateful that the Administration is pursuing the coated paper case.

I think this is an important, groundbreaking initiative, and essential, if we are to get China to operate within the rules-based framework that we had always understood was the intent of bringing them into the WTO.

I'm—with that, Mr. Chairman, I'm grateful for the opportunity to have asked these questions, and I'll yield back my time.

Chairman LEVIN. Thank you. Thank you for your salient questions.

Mr. Meek, do you wish to interrogate, or catch your breath?

Mr. MEEK. Are we talking about—you said interrogate. Are we——

Chairman LEVIN. Mr. Spooner.

Mr. MEEK. Are we in China or are we in the United States? No? Okay. All right. Great.

Mr. Spooner, I—actually, I walked in from the vote, and I left my folder, but I know you may be familiar with the bill that Representative Ryan is sponsoring, and there's a lot of discussion about what China does with its dollar that works against U.S. companies.

You probably addressed this a little earlier, and I apologize, Mr. Chairman, for coming in a little delayed.

This is a major, major concern that I think overall, hurting trade, and hurting the outlook on trade that so many Americans met with some level of enthusiasm, thinking that it would be good for U.S. business and it would be good for small businesses, and now finding, U.S. businesses are finding that, as relates to competition, that they're at a disadvantage because they keep moving, changing the rules in China as relates to the dollar and subsidizing companies there.

I say all of that in a global sense, to say that being on the Subcommittee on Trade, being from South Florida, where we have hopefully, if we can resurrect a free trade agreement (FTA) experience down there, and also being the financial center for the Americas and the music capital and music capital, what have you, it's like a doormat for trade.

Now we're having political problems. So, many Members of Congress have been elected, especially in the last cycle, running against China, running against trade agreements.

I came to talk in a very detailed way about the China bill, but—that Mr. Ryan has, and is also sponsored in the Senate, but I wanted to hear some of your feelings on what can be done.

Mr. SPOONER. Thank you, Congressman.

I suppose what's commonly referred to as the Ryan bill, or the Hunter-Ryan bill would, if I remember correctly, stipulate that China's currency practices are—fit the definition of a subsidy that would be countervailable [sic] under our domestic law.

I frankly can't comment on whether or not the Administration supports the bill. We sort of prepped today for H.R. 1229.

I can tell you that, should Commerce be presented with a set of facts or a petition in which the alleged activity meets the definitions of a subsidy under our domestic law, that it be a government policy that provides a specific benefit to an industry, that harms U.S. producers, we would do what we could to countervail it.

Mr. MEEK. Well, I—that bill is almost the embodiment of what—especially being—if you're from Ohio or South Carolina or any of these States that have been heavily affected by trade, then you would be for this, be for the Ryan bill.

I think that it would be good if you all can continue to have good dialogue on where you can come together, because I think something is going to happen in the 110th Congress. The will and the desire is there to make it happen.

Mr. Chairman, I just wanted to come because I know that that legislation may very well be coming before either our Subcommittee or our Committee if we decide to take it on, and it's something that is, in my opinion, technical, because I've read the bill and, as you know, Congressman Ryan and I work very closely together.

He reminds me every day that he's an appropriator and he's more important than I am. So, I——

Chairman LEVIN. Don't buy that.

Mr. MEEK. I don't buy it. I just told him on the Appropriations Committee he has maybe 80-something Members. I said, "I know all of the Members on my Committee. Do you?"

So, we just leave it like that.

It's such a—putting all jokes aside, it's such a technical and serious piece of legislation, so many lives have been affected by it, I just wanted to come to ask you today, and your staff, to hopefully work with us on something that can hopefully level the playing field.

Thank you, Mr. Chairman.

Chairman LEVIN. Thank you for raising it. It isn't the subject matter today, but it is very much related, Mr. Meek.

Our Subcommittee has been talking to the Financial Services, the appropriate Subcommittee, and we may well hold a joint hearing between our two Committees.

So, I think you're right, the currency issue is inescapably before us.

Mr. MEEK. We're just trying to build the will and desire here in the halls of Congress to deal with it and deal with it in a very appropriate way that won't hurt our efforts in China, but won't continue to hurt U.S. companies here.

Thank you.

Chairman LEVIN. All right. Well, I think that's it, Mr. Spooner. Thank you very, very much, and again, thank you for your patience.

Mr. SPOONER. Thank you.

Chairman LEVIN. All right. The next and last panel will come forth.

I'll introduce the panel as you're being seated.

I think we'll take them in this order:

John Comrie, who is director of trade policy, government affairs, and communications for IPSCO Steel in Illinois.

David Phelps, who is president of the American Institute for International Steel.

Usha Haley, who is an assistant professor of management and director of the Global Business Center, University of New Haven, New Haven, Connecticut.

Daniel Porter, who is a partner in the International Trade Group, Vinson & Elkins.

James Hecht, who is a partner, international trade practice, at the firm of Skadden Arps.

Let me, as you begin, and if you would, in that order, thank you for providing the testimony as the rules provide but are not always implemented, and that is, you were able to submit them, I think, in each case yesterday, and that gave us a chance last night and this morning to read them over.

My guess is that many of the Members, if not all, having had this material, were able to take a look at it, and surely their staffs were, before this hearing.

So, thank you very much for coming. Thank you very much for your patience.

We now await eagerly your testimony.

Mr. Comrie.

STATEMENT OF JOHN COMRIE, QC, DIRECTOR OF TRADE POLICY, GOVERNMENT AFFAIRS AND COMMUNICATIONS, IPSCO STEEL AND IPSCO TUBULARS, LISLE, ILLINOIS

Mr. COMRIE. Thank you very much, Mr. Chairman.

It's my pleasure to be here this afternoon.

Mr. Chairman, and Members of the Committee on Ways and Means Subcommittee on Trade, my name is John Comrie and I am the director of trade policy and communications at IPSCO.

I appreciate the opportunity to testify in support of H.R. 1229, the Nonmarket Economy Trade Remedy Act of 2007, as introduced by Representative Arthur Davis and Phil English.

I am testifying today on behalf of IPSCO, but I believe that my views are shared by the U.S. steel pipe and tube manufacturing industry, the Greater U.S. steel industry, and the many employees that are affected by unfairly traded imports from nonmarket economy countries, particularly the People's Republic of China.

I am here as a member of a company and a member of an industry that competes successfully against any in the world, as long as all producers are playing by the same rules.

As one of North America's leading steel plate and pipe producers, IPSCO is uniquely positioned within the marketplace for long-term sustainable growth.

Despite being a well-managed and highly efficient global competitor, more and more IPSCO finds itself being undercut by Chinese-produced oil country tubular goods (OCTG) pipe products that are crucial for oil and gas exploration.

Neither the Chinese steel nor the pipe industry has natural resource advantages over anything in the U.S. industry, and in fact, has to overcome several such disadvantages.

China's government subsidies have been central to the building of the Chinese steel industry.

The combination of pervasive State ownership, direct and indirect subsidies, other government support, and a longstanding development policy based on targeted exports allows Chinese OCTG pipe products to be produced and sold below their actual value.

As my testimony today only can provide a brief summary of China's government subsidies to its steel industry, I would like to direct you to my written testimony for a more complete statement.

In 2006, China produced 423 million metric tons of steel which was more than the United States, the European Union, and Japan combined.

In recent years, capacity expansion efforts have increasingly been directed toward higher value-added steel products, such as corrosion resistant steel and OCTG.

The extraordinary and unprecedented expansion of China's steelmaking capacity is a function of decisions by government planners coupled with the mobilization of massive resources to carry them out.

In 1990, China's steel industry was technologically lagging, inefficient, and incapable of satisfying the country's rapidly growing demand for steel.

Therefore, in the mid-1990s, the Chinese government decided to promote the steel industry as a national priority.

The steel enterprises, implementing the government's expansion plans, were overwhelmingly government owned. Many were poorly suited to be self-sustaining steel producers. Financing of these enterprises was mainly derived from government investments and loans.

Thus, it was not surprising that, by the end of the 1990s, many Chinese steel mills had fallen into dire financial straits.

In the United States, such a situation would have resulted in bankruptcy, liquidation, or at least mill closures.

In China, however, failing enterprises continued to expand capacity based on government write-offs of bad debt and additional injections of State-sponsored capital.

The Chinese government's financial support to the steel industry has countless more aspects, all of which are detailed in my written testimony.

The enactment of H.R. 1229 is essential to ensuring free and fair trade. The legislation would ensure that our nation's fair trade laws are uniformly applied to all prohibited trade subsidies, regardless of the country of origin.

The bill would make clear that the countervailing duty laws shall be applied to nonmarket economies.

It would recognize the importance of congressional consideration of whether a country's nonmarket economy status should be revoked without unduly burdening Commerce's ability to administer our nation's trade laws.

Finally, it would require the International Trade Commission (ITC) to undertake a comprehensive study of China's use of unfair and injurious subsidies.

Finally, Mr. Chairman, I'd like to conclude my remarks based on a couple of my own personal experiences.

I have for some time, like many others, been trying to understand what is going on in China. It's obviously a major force in the world.

I have been to Beijing, I've participated in the U.S.-China steel dialogue.

My company has hired a prominent Washington trade firm to make an investigation of subsidies in the steel and the OCTG industry, and we have made many efforts to try and understand what's going on in China.

This bill would provide the opportunity to bring cases which would lead to serious investigations by the Department of Commerce.

These investigations will gather information that only a Government agency can obtain. Nothing in this bill prejudges the results of those investigations.

Finally, the bill provides for annual updates on that information.

All of those actions would help solve this issue of transparency.

It is the underlying feature of the bill, is that it would promote an openness of what's going on in China. It would allow people around the world, and particularly in this country, to understand what's going on in China.

Thank you for providing me the opportunity to testify today. I am happy to respond to any questions the Members of the Committee may have.

[The prepared statement of Mr. Comrie follows:]

Prepared Statement of John Comrie, Q.C., Director of Trade Policy, Government Affairs, and Communications, IPSCO Steel and IPSCO Tubulars, Lisle, Illinois

Mr. Chairman and Members of the Committee on Ways and Means Subcommittee on Trade, my name is John Comrie and I am the Director of Trade Policy and Communications at IPSCO. I appreciate the opportunity to testify in support of H.R. 1229, the Nonmarket Economy Trade Remedy Act of 2007, as introduced by Representatives Artur Davis and Phil English on February 28, 2007. I thank Representatives Davis and English for introducing this important legislation and Chairman Sandy Levin for calling this hearing today.

I am testifying today on behalf of IPSCO, but I believe that my views are shared by the U.S. steel pipe and tube manufacturing industry, the greater U.S. steel industry and the tens of thousands of the workers directly and indirectly affected by unfairly traded imports from nonmarket economy countries, particularly the People's Republic of China ("China"). I am here as a member of a company and a member of an industry that competes successfully against any in the world, as long as all producers are playing by the same rules. I am here to request your assistance in leveling the playing field and supporting the domestic steel industry and its employees at what they do best, compete and win.

Both Goldman Sachs and steel industry associations describe IPSCO as one of North America's leading steel plate and pipe producers. Due to its state-of-the-art facilities, management experience, and focus on high quality, low-cost production, IPSCO is considered to be uniquely positioned within the marketplace for long term sustainable growth. Although IPSCO started as a Canadian company, by relocating our headquarters to Chicago, Illinois in 1999, building two modern steel mills in Alabama and Iowa and acquiring The NS Group in 2006, IPSCO cemented its long standing dedication and investment in the health and vitality of this critical U.S. industry as well as the entire U.S. economy. Currently, IPSCO owns and operates 16 mills and plants throughout the central states of Minnesota, Iowa, Nebraska, Okalahoma, Kentucky, Alabama, Arkansas, Pennsylvania, and Texas. Each day in these states, more than 2800 people provide the labor necessary for IPSCO to operate. The jobs as well as other businesses indirectly dependant upon IPSCO leads to an additional 20,000 U.S. jobs using the multiplier of 7:1 commonly associated with the steel industry. We have invested more than $1 billion in our U.S. facilities over the past ten years and this year again, plan to make major capital improvement expenditures to insure IPSCO remains the globally competitive company it is today. IPSCO is a proud and active member in each of the communities in which it operates, contributing significantly both financially and as volunteers to community based organizations.

Despite being a well managed and highly efficient global competitor, more and more, IPSCO finds itself being undercut by Chinese produced oil country tubular goods ("OCTG"), pipe products that are crucial for oil and gas exploration. Since 2002, Chinese exports of OCTG pipe to the United States increased by approximately 1000%.[1] This is despite the fact that China has no natural advantages with regard to steel production. In fact, China must overcome several natural disadvantages including the high cost of energy and a shortage of water resources. As I will explain later, the combination of pervasive state ownership, direct and indirect subsidies, other government support, and a long standing development policy based on targeted exports allows Chinese OCTG pipe products to be produced and sold below their actual value. The resulting playing field is neither level nor fair.

In accepting China into the WTO, provisions were incorporated to address surges of Chinese products into the U.S. market, notably Section 421. The domestic pipe

[1] According to Chinese Customs Statistics, 2002–2006 Chinese OCTG exports to the United States grew by 843%. U.S. import data show imports of Chinese OCTG pipe grew by 1083% for the same period.

and tube industry put forth a very strong Section 421 case before the International Trade Commission and the ITC approved the industry's position. Unfortunately, however, the Administration declined to provide relief. With such discretionary authority built into the statute, obtaining relief under Section 421, no matter how strong the case, is entirely uncertain.

The simple fact is that highly efficient and industry leading producers such as IPSCO can only counter the subsidies our Chinese counterparts receive with actions under U.S. fair trade laws. WTO-sanctioned trade remedy laws must be allowed to operate effectively to properly offset these subsidizes and discourage future market-distorting subsidization by governments in nonmarket economies, including China.

Government Subsidies Have Been Central to the Building of the Chinese Steel Industry

Since 1990, China has been the site of the largest expansion of steelmaking capacity in history, the sheer scale of which defies superlatives. In 1990, China produced 66 million metric tons of steel, or less than the United States, the European Union or Japan. Sixteen years later, in 2006, China produced 423 million metric tons—a more than six fold increase over 1990, and more than the United States, the European Union (the "EU") and Japan *combined* produced. The China Iron and Steel Association ("CISA"), which has always underestimated output growth in the past, is projecting that Chinese steel production will surpass 470 million metric tons in 2007 and perhaps be as high as 480 million metric tons. In recent years, capacity expansion efforts have increasingly been directed toward higher value-added steel products, such as corrosion-resistant sheet and OCTG.

The extraordinary and unprecedented expansion of China's steelmaking capacity is a function of decisions by government planners, coupled with the sustained will and the mobilization of massive resources to carry them out. In 1990, China's steel industry was technologically lagging, inefficient, fragmented, and incapable of satisfying the country's rapidly growing demand for steel, and China was dependent on imports for many of its steel needs. The central government decided to promote the steel industry as a national priority, manifested in the Ninth Five Year Plan (1996–2000) and in subsequent plans. Promotion of the steel industry was also emphasized in the five-year plans of many of China's provinces and municipal governments—in many cases specifying particular production lines which were to be established or expanded, steel products whose production was to be increased, and types of equipment which were to be installed. For example, in 2006, the 11th Five Year Plan for the Inner Mongolia Autonomous Region provided that "in the iron and steel industry [we shall] accelerate the Hexi Industrial Area . . . focus on promoting the projects including the 3 million metric tons automobile sheet project of BaoTou Steel, the 2 million metric tons seamless steel project of Huaye Special Steel, the 2 million metric tons special seamless steel project of Mengfeng. . . ."[2]

The steel enterprises which were expected to implement the government's expansion plans were themselves overwhelmingly government owned, and, in cases like that of Tianjin Pipe, China's largest producer of OCTG, were expressly created as "key projects" by the government for the specific purpose of producing strategically important steel products. Financing of these projects was derived from equity infusions by government investment corporations; low interest loans from government banks, and foreign loans utilizing Chinese central, regional and local government development entities as financial intermediaries. Typically, in 2000 the State Administration of the Metallurgy Industry ("SAMI") announced plans to spend over $6 billion "to ensure that the steel industry can compete in world markets after China enters the World Trade Organization. . . . Nearly 28 billion yuan ($3.4 billion) of the spending will be in the form of low interest bank loans."[3] The government is in effect, through the various enterprises which it owns and controls, both the borrower and the lender, and not surprisingly under such circumstances, the expansion of China's steel industry has never faltered for shortage of capital.

From a market-based economic perspective, many of China's steelmaking expansion projects were irrational—poorly sited, unsuited to actual market demands, and unlikely to ever be self-sustaining. By the end of the 1990s many new or expanded mills had fallen into financial difficulty and a vast portfolio of loans which had been made to such entities became "nonperforming," e.g., the enterprises were no longer able to make principal and interest payments on the basis that had been established

[2] Inner Mongolia Autonomous Region Developmental Reform Commission, *11th Five Year Plan on Regional Economic Development of Huhehaote, BaoTou, and Erdos in Inner Mongolia Autonomous Region* (posted July 17, 2006) (translation from Chinese).

[3] Gong Zhengzheng, "Steel Gets Support for Upgrades," *China Daily Business Weekly* (March 12, 2000).

when the loan was made. For a private company in a market economy, such a situation is an existential crisis which often culminates in bankruptcy, liquidation, and the closure of a mill. In China, however, failing enterprises continued to invest heavily and expand capacity. Government banks wrote off massive quantities of bad debt, and when doing so threatened their own solvency, themselves received injections of capital from the government. Pursuant to so-called "debt-to-equity swaps," banks transferred their bad loans to state-owned asset management corporations, which converted "debt" to "equity." Because in virtually all of these cases the government—through one or another subordinate entities—owned the enterprises both before and after the "swaps," it is unclear what, if anything, it gained by these transactions; the enterprises however, had their debts erased and were in a position to resume borrowing in order to carry out the next phase of expansion. One of China's largest steel producers, Anshan Iron and Steel, fell into "dire straits" in the late 1990s as a result of losses and a heavy debt burden, but the government and government banks "continue[d] to supply it with resources and capital." Anshan continued to invest heavily in expansion and modernization with "state banks . . . providing most of the funds for the modernization drive."[4]

National and local governments have used financial incentives to induce mergers of steel mills to create enterprises of larger scale. In 1999 the government announced that the Industrial and Commercial Bank of China (the "ICBC") would "play an important part in restructuring the metallurgy industry by adjusting its credit policies," including "debt-equity swaps, writing off non-performing loans and granting closed-end credit to boost restructuring of the industry." The ICBC was to give "special support" to mergers involving Bao Steel, Anshan and Shougang Steel to "sharpen their competitive edges in the international market and help one or two of them claw to the world top 500 companies list."[5] The mergers, unlike consolidations of private companies, were often not undertaken on the basis of management initiative but command-style decisions by government officials. According to one study on the mergers, "the companies concerned had to go along with the plans of the central administration, [and therefore] sought to anticipate the wishes of the government, which in any case would have been imposed on them."[6] In 2000 executives of Baosteel reported that Chinese Premier Zhu Rongji had compelled the company to absorb the Shanghai Yichang Sheet Company and "instructed Baosteel to make Yichang profitable." To sweeten the transaction the State Council (led by Zhu) provided $83 million in low interest loans.[7]

Government decisions and government financial support are providing the basis for an extraordinary expansion of capacity in China's OCTG industry. China has become a net exporter of OCTG products in recent years as production has rapidly outpaced domestic consumption. Yet a number of its OCTG producers are significantly expanding capacity. Like China's steel industry generally, the OCTG sector is dominated by majority state-owned enterprises, which account for over two-thirds of China's OCTG production. The central and many regional governments have concluded that because of its relationship to the energy sector, OCTG is a "strategic" or "pillar" industry warranting priority support.

Tianjin Pipe, China's largest producer of OCTG with nearly 30 percent of China's OCTG capacity, illustrates the close relationship between governments and the OCTG industry. Although, Tianjin Pipe is owned by a number of organizations, virtually all of the owners are governmental organizations. Tianjin Pipe was conceived as the so-called "Big Seamless Pipe" project during the Eighth Five Year Plan in the early 1990s; its establishment was the "strategic decision of the Party and State" to end China's dependence on OCTG for the domestic energy industry. Tianjin Pipe was capitalized entirely by debt arranged under various government auspices. Particularly important was the role of the Tianjin International Trust Investment Corp. ("TITIC"), a municipal government entity which borrowed hard currency abroad and reloaned the funds to local industrial projects including the "Big Seamless" project. By 1998–99, fully 40 percent of all of TITIC's outstanding loans were extended to one enterprise, Tianjin Pipe. TITIC, although a governmental entity, suffered a downgrading of its credit rating, in large part because of its exposure to its loans to Tianjin Pipe, which by the mid-1990s was on the verge of default. The City of Tianjin resolved the problem with injections of funds into Tianjin Pipe,

[4] "Friends in High Places," *Far Eastern Economic Review* (April 29, 1999) p. 68.
[5] "Bank Set to Support Industry Restructuring," *China Daily* (December 7, 1999).
[6] Jean-Francois Huohet, "Concentration and the Emergency of Corporate Groups in Chinese Industry," *China Perspectives* (May-June 1999) p. 16.
[7] "Gearing Up for Battle," *Asiaweek* (December 22, 2000); "A Profile of the Steel Industry in China," *Metal Bulletin* (February 2000).

enabling it to continue to service its debt to TITIC (itself an instrumentality of the City of Tianjin).

By the mid-1990s Tianjin Pipe was burdened with over $1 billion in debt and was losing money on its operations. Nevertheless the government decided that it should continue to expand by opening a second production line, with officials pointing out that "oil casing [OCTG] is a strategic product." The government agreed to inject 4 billion yuan into the company (about $450 million). The company pressed ahead with expansion, ultimately becoming the largest producer of OCTG in China. In 2003 an official of the Tianjin Municipal Government said in a speech to the Tianjin Municipal Peoples' Congress that

> It is necessary for the steel pipe company [Tianjin Pipe] to continue to develop new products, expand the scale of production, and build itself into a large comprehensive enterprise that ranks side by side with three other top steel pipe manufacturing enterprises of the world.[8]

In 2006, Tianjin Pipe announced plans to expand capacity to enable it to triple its annual output by the end of 2008.

Direct financing from state-owned banks, investment corporations, or financial intermediaries represent only one aspect of government financial support to the steel industry. Many steel enterprises fall into arrears on their tax payments and the national and regional governments periodically forgive the arrearages. The government plays an active role in among other things controlling the prices of raw materials to the steel industry to the industry's advantage; grants are provided by the central government to defray interest payments and to pay for energy and raw materials. A sweeping array of local benefits, including concessional rents and utilities rates, are available to steel enterprises which are located in designated industrial parks. The central government has periodically intervened in the market when steel prices have fallen, encouraging and in some cases imposing cartel arrangements on the steel industry to stabilize and lift prices.[9]

Enactment of the Nonmarket Economy Trade Remedy Act of 2007 Is Essential to Ensuring Free and Fair Trade

I. *Application of Countervailing Duties to Nonmarket Economies*

First, H.R. 1229 would make clear in our nation's fair trade laws that the countervailing duty laws shall be applied to nonmarket economies. The legislation would ensure that our nation's fair trade laws are uniformly applied to all prohibited trade subsidies, regardless of the country of origin. This relief is vital to the ability of U.S. manufacturers and producers to effectively compete on a level playing field against unfairly-traded imports, particularly from nonmarket economies such as China.

In 1984, the administering authority for our nation's fair trade laws, the U.S. Department of Commerce ("Commerce"), made a policy decision to forgo application of countervailing duties to nonmarket economies based on its perceived definition of a "subsidy" as any action that distorts the market process. Based on that definition, Commerce determined it was impracticable to identify a specific subsidy in a nonmarket economy. The U.S. Court of Appeals for the Federal Circuit in *Georgetown Steel* subsequently upheld Commerce's policy decision, but emphasized that the policy is completely discretionary; it is not required by international law, U.S. statutory law, or even Commerce's own regulations. The court simply deferred to the rationale of the administering authority.

In the twenty plus years since Commerce's flawed policy decision, there have been changes in U.S. and international law and market conditions that now mandate the application of countervailing duties to nonmarket economies. In 1994, the World Trade Organization (the "WTO") Agreement on Subsidies and Countervailing Measures (the "SCM Agreement") established a clear and administrable definition of "subsidy" that encompasses nonmarket economies. Specifically, the SCM Agreement states that a countervailable "subsidy" shall be deemed to exist if an administering authority makes all of the following findings: (1) there is a financial contribution by a government or public body, (2) in the form of an income or price support, (3) where a benefit is conferred, (4) to a specific enterprise or industry. This standard has been enacted into U.S. law as part of the Uruguay Round Agreements Act.

Based on the correct standard for the finding of a "subsidy," Commerce's original rationale has been completely contradicted. A countervailable subsidy is not defined by the effects it has on a nonmarket economy, but instead is defined by the actions

[8] "Government Work Report Delivered by Dai Xiangbong at the First Session of the 14th Tianjin Municipal Peoples' Congress on January 18, 2003" reproduced in *Tianjin Ribao* (January 27, 2003).

[9] "China's Iron and Steel Pricing Agreement," *Gendai Chuyokai* (September 2000).

taken by the exporting government. It is no wonder that Canada has used the SCM Agreement standard to apply countervailing duties to China without revoking China's nonmarket economy status for several years now.

Commerce itself has recognized the flawed rationale of its 1984 policy. In 1991, Commerce initiated a countervailing duty investigation of electric fans from China. Recently, in November 2006, Commerce initiated another countervailing duty investigation against China, this time for imports of coated free sheet paper. As part of its investigation, Commerce has stated that it currently is reevaluating its policy of excluding nonmarket economies from our nation's countervailing duty laws. While we commend Commerce for undertaking this initiative, the time for Commerce's deliberation is over due. It is time for Congress to act.

Fundamentally, no country or industry should be automatically exempt from our nation's fair trade laws. If an exporting country—market or nonmarket—is unfairly subsidizing its manufacturers to the injury of a U.S. domestic industry, Commerce must apply countervailing duties to remedy this injury. Countries like China should not be allowed a free pass from the U.S. fair trade laws simply because of its nonmarket economy status.

Specifically for China, H.R. 1229 would establish a method for determining the benchmark from which Commerce would be able to identify and quantify China's prohibited trade subsidies. So long as China remains a nonmarket economy, the bill would require Commerce to presume that the terms and conditions prevailing in China are not practicable for the identification and calculation of a countervailable benefit. As such, Commerce would be required to use the terms and conditions prevailing outside China. By looking to the terms and conditions prevailing outside China, Commerce will be able to better quantify the benefits received by Chinese manufacturers and exporters.

The bill also takes into consideration the fact that China will be allowed market economy status by December 11, 2016, as agreed upon in China's WTO accession protocol. When China reaches market economy status, the bill will allow Commerce to take into account the possibility that the terms and conditions prevailing in China at that time may not be the appropriate benchmark. While Commerce is directed to first consider China's prevailing market conditions, the bill gives Commerce the authority to look outside China if the situation so warrants. This authority is vital because an artificial deadline established by the WTO is by no means an accurate indication of China's true market economy conditions.

II. *The Importance of Congressional Approval*

Second, H.R. 1229 would recognize the importance of Congressional consideration of whether a country's nonmarket economy status should be revoked without unduly burdening Commerce's ability to administer our nation's fair trade laws. The bill requires any final determination by Commerce to revoke a nation's nonmarket economy status to have the approval of Congress through a joint resolution. Specifically, the President must notify this Committee and the Senate Committee on Finance no later than ten days after the publication of Commerce's final revocation determination in the Federal Register. Congress must then introduce a joint resolution approving or disapproving Commerce's final revocation determination.

Like the President's fast track authority, the bill has an expedited debate and approval process. Amendments to the joint resolution and motions to postpone consideration are not allowed. There is a defined and expedited period for committee and floor consideration. Thus, the President can rest assured that Congress will not be able to unduly delay the revocation of a nation's nonmarket economy status. The involvement of Congress is purely to ensure that Commerce has made the right decision with respect to our nation's fair trade laws.

The importance of Congressional approval for revocation of nonmarket economy status is most evident in the current situation with China. Even though China agreed to be classified as a nonmarket economy for a period of fifteen years after its accession to the WTO in 2001, the Chinese government has shown an eagerness to reach market economy status well before 2016. As we have shown today, China's efforts to gain market economy status are entirely premature, as it has yet to adhere to true market economy principles. China continues to provide subsidies to its steel exporters, it engages in currency manipulation, and it has not maintained necessary and appropriate labor and environmental standards. Despite all this evidence, there is considerable concern that China may be able to gain market economy status without undergoing true market reforms.

Thus, it is imperative for Congress to consider the decision of whether to allow China market economy status. As today's hearing proves, open and transparent discussions will lead to a more reasoned decision on trade issues involving China. U.S. manufacturers, workers and other concerned citizens should be allowed to voice their opinions on the devastating impact of Chinese imports on the U.S. economy, and these views must be taken into consideration if and when Commerce seeks to revoke China's nonmarket economy status. In no uncertain terms, the market economy status of a country is fundamental to the effective enforcement of our nation's fair trade laws.

III. *A Comprehensive Study of China's Use of Subsidies*

Finally, H.R. 1229 would require the U.S. International Trade Commission (the "Commission") to undertake a comprehensive study of China's use of unfair and injurious subsidies. The study would catalog, and whenever possible quantify, the practices and policies that China's central, provincial and local governments use to support and influence the decisions of Chinese manufacturers and industries. The Commission must report the results of its study to Congress and the public no later than nine months after the date of enactment of this bill, and annually there afterwards.

Critics of this bill have argued that it would be difficult to pinpoint the level of China's prohibited subsidies. The Commission's study and report would assuage these concerns by providing a systematic catalog of how China uses government intervention to promote investment, employment and exports. As we have shown, China has an established policy of providing prohibited subsidies to Chinese steel exporters and other industries. But our research efforts are limited; no one U.S. manufacturer or industry can track every subsidy China provides to its manufacturers and exporters. Thus, it is imperative that the U.S. government undertake an annual and comprehensive study of the terms and conditions prevailing in China. Only by holding the Chinese government accountable for its actions will China finally decide to undertake true market reforms.

Thank you for providing me the opportunity to testify today. I am happy to respond to any questions the Members of the Committee may have.

Chairman LEVIN. Thank you.

Mr. Phelps.

STATEMENT OF DAVID H. PHELPS, PRESIDENT, AMERICAN INSTITUTE FOR INTERNATIONAL STEEL (AIIS) AND MEMBER OF THE BOARD OF THE CONSUMING INDUSTRIES TRADE ACTION COALITION (CITAC)

Mr. PHELPS. Good afternoon.

I'm Dave Phelps, president of the American Institute for International Steel and a member of the board of the Consuming Industries Trade Action Coalition, CITAC.

CITAC's membership includes American manufacturers and retailers in a wide variety of industrial and consumer goods, from auto parts to household items.

We do not condone trade-distorting subsidies, neither AIIS nor CITAC, but any legislation or policy choice that affects competitiveness should consider the impact on consuming industries.

CITAC strongly opposes putting consuming industries in the United States at risk with H.R. 1229.

The bill before you would put American businesses and workers in jeopardy for the following reasons:

> First. It is fundamentally unfair to U.S. consuming industries. The bill offers no guidance to the Commerce Department in calculating subsidies in NMEs.
>
> Since Commerce cannot fairly and accurately calculate subsidies in nonmarket economy situations, the Department has declined to calculate them in the past.
>
> We are opposed to a sudden change in policy that would inevitably harm consuming industries in the United States.

Two. The WTO Subsidies Agreement prohibits double counting, but the bill fails to address double counting. Indeed, as we read 1229, double counting is practically required.

Three. H.R. 1229 would require congressional approval before the U.S. Government could declare that China's economy has graduated from NME status.

This requirement would turn what is now a technical and economic analysis done by the Department of Commerce into a political exercise.

Four. The bill creates an irrefutable presumption that information within China is not reliable.

This is unacceptable, because we have no assurances that information external to China is any more reliable.

We urge the Subcommittee to insist on the use of reliable information internal to the country under investigation and to require accuracy above retribution.

Five. Application of CVDs to nonmarket economies is probably WTO-illegal.

We believe that the WTO accession protocol with China does not permit the United States to impose CVDs on China while simultaneously treating that country as a nonmarket economy.

We, as well as China, must abide by our WTO commitments.

Six. Our current trade remedy laws contain fundamental inequities that often cause more harm than benefit. In our view, expanding existing trade remedy law is counterproductive until those inequities are taken care of.

For example, under current law, consuming industries and the public interest play no role whatsoever in determining whether ADs and CVDs are imposed.

The addition of countervailing duties to nonmarket economy cases, given the uncertainty of data and methodology for determining appropriate duties, will inevitably lead to excessive taxation of American industry.

This is a burden that our economy cannot afford in today's global marketplace.

We do not believe that American industry is under assault from deliberate dumping and subsidies.

In fact, the domestic steel industry posted all-time record profits in 2006, a year that posted record imports and record imports for companies in the domestic steel industry themselves.

Therefore, from the perspective of the consuming industries, we have a duty to all U.S. industries to calculate fairly and accurately these duties while determining equally carefully that the duties we decide to impose are in fact in the public interest.

We see significant reform in trade remedy laws needed, including:

> One. Industrial consumer standing. That's H.R. 1127.
>
> Adoption of prospective duty assessment so that importers know at the time of entry the amount of the definitive duty.
>
> Abolition of the unfair practice and illegal WTO practice of zeroing in anti-dumping investigations and reviews.

Seven. Finally, U.S. anti-dumping law already provides adequate remedies for U.S. producers who believe they are injured by imports from China.

The duties on steel products that are currently in place due to these nonmarket economy cases range on hot rolled coils from 65 to 90 percent, clearly high enough to knock them out, completely out of the market, and on plate, as high as 129, almost 129 percent.

In conclusion, we must make sure that trade remedy laws do not create more harm to the United States than benefit.

Given the inequities of our current trade remedy law and practice particularly with regard to U.S. consuming industries, the imposition of countervailing duties on China and Vietnam, the two major nonmarket economies with whom we trade extensively, would not be in the best interests of the U.S. economy. I would be happy to answer any questions you may have. Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Phelps follows:]

Consuming Industries
Trade Action Coalition

BEFORE THE COMMITTEE ON WAYS AND MEANS
Subcommittee on Trade

Testimony of David H. Phelps
Member of the Board, Consuming Industries Trade Action Coalition (CITAC)

Good afternoon. I am Dave Phelps, President of the American Institute for International Steel (AIIS) and a Member of the Board of the Consuming Industries Trade Action Coalition (CITAC). CITAC's membership includes American manufacturers and retailers of a wide variety of industrial and consumer goods, from auto parts to household items. Our member companies employ hundreds of thousands of workers and have a tremendous positive impact on the U.S. economy. I am pleased to appear before the Subcommittee today to talk about CITAC's position on the application of countervailing duties to non-market economies.

First, neither CITAC nor the AIIS condones trade-distorting subsidies. But we do not believe that this end justifies unlimited means. CITAC supports the right of all U.S. industries, manufacturers and retailers, to compete in the global economy and believes that any legislation or policy choice that affects competitiveness should consider the impact on consuming industries. In that vein, CITAC very much appreciates the opportunity to participate in today's hearing.

In short, while CITAC does not oppose the application of countervailing duties to offset injurious distortive subsidies under market economy rules, we strongly oppose putting consuming industries in the United States at risk with HR 1229. The bill before you would put American businesses and workers in jeopardy for the following reasons:

1. It is fundamentally unfair to U.S. consuming industries. Instead of import competition making American industry more competitive globally, it will make industries in other countries more competitive. The bill offers no guidance to the Commerce Department in calculating subsidies in non-market economies. Requiring the Department of Commerce to impose countervailing duties on China and other non-market economies will present Commerce with an intolerable burden; it cannot fairly and accurately calculate subsidies in situations the Department has never faced. Principally for this reason, the Department has declined to calculate countervailing duties for non-market economies in the past. Given this history, we are opposed to a sudden change in policy which would only result in increased

burdens and restrictions on consuming industries in the United States that rely on competitively priced imports if they are to succeed in the global marketplace.

2. The WTO Subsidies Agreement prohibits "double counting" of subsidies in the guise of antidumping duties. We do not see any prohibition on double counting in this bill, which we view as a significant problem. Indeed, as we read H.R. 1229, double counting is practically required. We cannot support a bill that does not explicitly address the issue of double counting.

3. H.R. 1229 would also require congressional approval before the U. S. government could declare that China's economy has graduated from non-market economy status. This requirement would wipe out decades of precedent and strip authority from the agency that is charged with administering these laws, turning what is now a technical and economic analysis done by the Department of Commerce into a political exercise.

4. The bill before the Committee essentially requires the use of third country information by creating an irrebuttable presumption that information within China is not reliable. However, we have no assurance that information external to China is more reliable. So we are faced with the likelihood of excessive imposition of duties on Chinese imports that will harm American manufacturers, retailers and consumers, based on unreliable information from a "surrogate country." We urge the Subcommittee to insist on the use of reliable information internal to the country under investigation, and to require accuracy above all else.

5. Application of countervailing duty laws to non-market economies is probably WTO-illegal. We cannot expect China and other WTO members to comply with their own WTO obligations if we do not. Moreover, we owe it to our own people to avoid WTO violations where possible. We believe that the WTO Accession Protocol with China does not permit the U.S. to impose countervailing duties on China while simultaneously treating that country as a "non-market economy" under antidumping rules.

6. Our current trade remedy law and practice contain fundamental inequities that often cause more harm than benefit. In our view, expanding existing trade remedy law is counterproductive until those existing inequities are fixed. For example, under current law consuming industries and the public interest play no role whatsoever in determining the imposition of often onerous and protective duties under the antidumping and countervailing duty laws. This inequity leads to the imposition of taxes, or duties, that raise raw material and input costs for American consuming industries. When those costs are artificially raised above the global price, American industries that rely on those products are made less competitive against their global

competitors. The addition of countervailing duties in non-market economy cases, given the uncertainty of data and methodology for determining the appropriate duties, will simply provide another opportunity for excessive taxation of American industry. This is a burden that our economy cannot afford in today's global marketplace.

We do not believe that American industry is "under assault" from deliberate dumping and subsidies, in fact, the domestic steel industry posted all-time record profits in 2006. Therefore, we have a duty to all U.S. industries to calculate fairly and accurately these duties while determining equally carefully that the duties we decide to impose are in fact in the public interest.

Accordingly, CITAC believes it is premature to make this precipitous change until the overall reform of these laws is a reality, including:

A. Industrial user standing, which would be provided by legislation currently pending before the House, H.R. 1127.

B. Calculation of duties so that importers know at the time of entry the amount of the definitive duty. Otherwise, uncertainty discourages fairly traded imports, and dampens legitimate competition.

C. Complete abolition of the WTO-illegal and unfair practice of zeroing which overtaxes American manufacturers, retailers and consumers.

Reform of the methodology for calculation of antidumping duties for non-market economies so that American manufacturers and retailers know that these duties accurately reflect any price discrimination in the U.S. market. Our current non-market economy procedures do not meet that test.

7. U.S. antidumping law already provides adequate remedies for U.S. producers who believe they are injured by imports from China. Indeed, 42 percent of U.S. antidumping cases initiated in 2006 were against China under the existing non-market economy rules. Furthermore, a special safeguard against imports from China was put into legislation (Section 421 of the Trade Act of 1974, as amended). On top of that, a textile-specific safeguard is in effect through 2008. Accordingly, with all these provisions in place, applying unfair, inaccurate and excessive countervailing duties to imports principally from China and Vietnam is not urgent.

CITAC believes U.S. trade remedy laws should work for all Americans. We must make sure that the imposition of trade restrictions is done judiciously, and that they do not create more harm to the U. S. economy than benefit. Given the inequities of our current trade remedy law and practice, particularly with regard to U. S. consuming industries, the imposition of countervailing duties on China and

Vietnam, the two major non-market economies with whom we trade extensively, would not be in the best interests of the United States economy. We strongly believe that such a step must not be taken without full knowledge of the adverse consequences on U.S. manufacturers, retailers and consumers. Once those consequences are considered, we are hopeful that the Congress will not approve this legislation in its current form.

I would be happy to answer any questions you may have.

Chairman LEVIN. Thank you very much.

Dr. Haley, welcome. Your turn.

STATEMENT OF USHA C. V. HALEY, PH.D., PROFESSOR OF INTERNATIONAL BUSINESS AND DIRECTOR, GLOBAL BUSINESS CENTER, UNIVERSITY OF NEW HAVEN, NEW HAVEN, CONNECTICUT

Dr. HALEY. Thank you, Chairman Levin, Members of the Committee, for the opportunity to provide my testimony in support of the Nonmarket Economy Trade Remedy Act of 2007.

My statement specifically focuses on on-the-book and off-the-book subsidies undertaken by the Chinese government in violation of its WTO commitments, the abilities of these subsidies to distort free markets and to hamper U.S. companies, and the remedial application of countervailing duties.

Why China?

China is the largest nonmarket economy. China is the nonmarket economy with the greatest commercial influence on the United States.

The U.S. trade deficit with China is the largest in trade history, and is growing. Pervasive subsidies seep through China, distorting markets and resulting in the misallocation of resources.

The WTO requires annual notification from members on subsidies they maintain and encourages additional needed information on subsidies.

On April 13, 2006, China submitted an overdue subsidies notification to the WTO in which it identified 78 subsidy programs from 2001 to 2004.

Table 1 in my written testimony specifically identifies the breakdown. However, for this presentation I have identified a top ten list of the beneficiaries of these subsidies in China's 2006 notification.

Foreign invested enterprises and foreign equity joint ventures, and agriculture and animal husbandry top the list. There are also several industry specific subsidies, including those aimed at integrated circuits, tea, copper refining, casting, forging, dies, and machine tools, specifically.

China's notification of its subsidy programs is incomplete. Generally, it concentrates on foreign invested enterprises and ignores local producers.

It also concentrates on the central government's programs and ignores provincial and municipal governments' programs.

It ignores most of the export and import substitution subsidies that I list in my testimony, and it provides no data or statistics on the amounts of subsidies or the effects on trade.

My research over the last eight years has shown that the Chinese government uses at least 15 types of different subsidies, and in my written testimony I identify a list of them, ranging from free to low-cost loans to the undervalued currency, and I can just go over a few examples here.

Free to low-cost loans is one subsidy. Half of all bank loans go to State-Owned Enterprise (SOEs). Most of these loans will never be repaid.

If the borrowers cannot pay back the subsidized loans, the banks convert the debt into equity in the SOEs or domestic companies.

Asset injections is another example. The SOE's parent companies, usually municipal governments or ministries, provide them with opportunities to acquire State-run businesses such as toll bridges at highly preferential terms.

Labor controls provide yet another example. The government exercises various methods to control employees, including the "dang'an" or employment dossier, and to reduce labor costs through injection of part-time and migrant workers.

The government also provides exemptions from mandatory worker benefits contributions to companies that satisfy certain export performance requirements.

On and on.

Lack of transparency reduces our ability to gauge the effects of subsidies.

It also reduces our abilities to gauge the true efficiency and productivity of Chinese labor.

It reduces the ability of U.S. manufacturers to prove dumping.

It magnifies the weaknesses of China's statistical system.

It reduces the credibility of the SOE's books, some of which have at least four different sets of books.

Lack of transparency specifically affects China's gross domestic product (GDP) figures; statistics generated by the National Statistics Board (NSB); sensitive data, such as those dealing with debt or foreign direct investment (FDI); statistics in private and service sectors; some economic and industrial data that the Chinese government classifies as state secrets; unemployment statistics; and statistics on non-performing loans (NPLs).

The 11th Five-Year Plan that has been revealed indicates that subsidies will flow into integrated circuits and software; new-generation networks; advanced computing; biomedicine; civil airplanes; satellite applications; high-performance and new materials, subsidies will also go into controversial sectors such as stem cells, gene therapy, and genetically modified crops; traditional U.S.-dominated industries, including software, semi-conductors, and space exploration; and renewable energy sources, such as solar, hydro, and wind power.

Subsidies are very difficult to understand and unravel, primarily because they are politically motivated—rather than economically motivated—and so they promote exports of inefficient domestic industries.

They're also guided by the need to control SOEs more effectively rather than to increase their profits.

They stem from long and mid-range plans as well as from mistakes. Though very difficult to unravel, they are clearest for global champions, such as PetroChina, and they are different at central, State, and local levels.

One example of the market distortion effects of subsidies is evident in the profits of foreign companies operating there.

Our research has shown that only one-third of the foreign invested enterprises in China have ever made a profit there.

United States companies operating in China had lower profit margins than in their global operations.

In 2004, total China earning for U.S. foreign affiliates, including all sources of profits, was $8.2 billion.

In 2004, U.S. foreign affiliates earned $7.1 billion in Australia, $8.9 billion in Taiwan and South Korea, and $14.3 billion in Mexico, with much smaller economies.

Five U.S. companies accounted for a third of the equity profits, showing that they're highly concentrated.

Comparisons can be made between subsidized and market-determined prices. Despite China's opacity, benchmarks, physical activity indices, and independent surveys can provide independent estimates of some subsidies.

Several corporations engage in these activities.

WTO provisions require that China divulge more information on the magnitude and effects of its subsidies.

What will countervailing duties do in China, and with China?

Countervailing duties will probably underestimate the amounts required to offset China's pervasive subsidies. However, small and medium-sized enterprises will find countervailing duties less onerous and more accessible than anti-dumping measures.

Countervailing duties will also give U.S. companies an explicit import relief measure that targets unfair government subsidies.

Countervailing duties therefore provide a credible and cost-effective way to offset some of China's subsidies and to level the competitive playing field. Half a loaf is better than no bread.

Thank you.

[The prepared statement of Ms. Haley follows:]

Prepared Statement of Usha C. V. Haley, Ph.D., Professor of International Business and Director of the Global Business Center, University of New Haven, New Haven, Connecticut

Thank you Trade Subcommittee Chairman Levin and honorable Members of the Committee on Ways and Means, for the opportunity to address such a distinguished and thoughtful group. I am a business professor and researcher who has studied nonmarket economies for close to three decades. My testimony stems from research that I have conducted over the last eight years on China's business environments, some of which has been published in my book, *The Chinese Tao of Business: the Logic of Successful Business Strategy* (John Wiley & Sons).

My statement specifically focuses on on-the book and off-the book subsidies undertaken by the Chinese government in violation of its World Trade Organization (WTO) commitments, the abilities of these subsidies to distort free markets and to hamper U.S. companies, and the remedial application of countervailing duties (CVDs).

China remains the largest nonmarket economy and the one with the greatest commercial influence on the USA. Trade with China comprises 12 percent of U.S. total trade. Yet, the equation appears highly unbalanced. U.S. exports to China in the first 11 months of 2006 exceeded $50 billion, up about 20 percent from the previous year and up over 163 percent from 2001 when China joined the WTO. Conversely, the U.S. goods trade deficit with China in 2006 should reach one-quarter of a trillion dollars—the largest trade deficit in U.S. history. U.S. imports from China have risen since China joined the WTO; simultaneously, imports from other East Asian countries have dropped $10 billion, hinting that Chinese products enjoy a highly-subsidized cost advantage.

The WTO requires annual notification from members on subsidies they maintain and encourages additional, needed information on subsidies. On April 13, 2006, China submitted an overdue subsidies notification to the WTO in which it identified 78 subsidy programs from 2001–2004. The WTO also specifies that members should provide sufficient information "to enable other members to evaluate the trade effects and to understand the operation of notified subsidy programs." China's report stated that several central government ministries and agencies distributed and monitored subsidies, and extensive legislation in China supported the subsidies. Yet, surprisingly, no statistical data existed in China to assess the trade effects of any subsidy or even the total annual amounts budgeted to these subsidies. Table 1 identifies the stated beneficiaries of China's subsidy programs from 2001–2004: Foreign-Invested Enterprises (FIEs)/Foreign Equity Joint Ventures and Agriculture/Animal Husbandry appear as the primary beneficiaries.

China's overdue notification of its subsidy programs to the WTO remains incomplete. Generally, the subsidy notification:

- Concentrates on subsidies to FIEs to invest in key strategic Chinese sectors and ignores most subsidies that reduce local producers' operating and production costs vis-à-vis foreign producers;
- Concentrates on subsidy programs supported by the central government and ignores all programs offered by provincial and municipal governments or the Peoples Liberation Army (PLA) in China;
- Ignores the subsidy effects of maintaining a cheap currency, as well as subsidies in several sectors including Commercial Banking lending policies or other financial preferences.

China's refusal to adhere to WTO compliance efforts stems in part from its inability to accept the key WTO principles of market access, non-discrimination and national treatment. Additionally, market mechanisms in China remain undeveloped, making its trade regime unpredictable and opaque. Although China implemented some key reforms, it has continued to use an array of industrial policy tools to promote or to protect favored sectors and industries, and these tools at times collide with China's WTO obligations.

Industrial subsidies in China derive from governmental dominance of the economy and from various factors including the central, provincial and municipal governments' strategic goals, patronage, and corruption. The subsidies include direct and indirect components that affect top and bottom lines of industrial operations, distort markets and misallocate resources.

Forms of Subsidies

State subsidies primarily flow into State-Owned Enterprises (SOEs) although some well-connected private firms also benefit from indirect subsidies such as Special Market Information. Currently, the state controls about half the industrial output and SOEs still account for 35 percent of urban employment. Almost all of China's heavy industry and much of its technology lies in governmental hands. The government controls about a third of China's economy through SOEs in key sectors such as defense and utilities. The State Owned Assets Supervision and Administration Committee (SASAC) directly manages the top 190 or so SOEs, the biggest of which have international stock-market listings.

Subsidies exist in all industries that the Chinese state and provincial governments considered economically or militarily strategic, including Resource Extraction, Steel, Computing, Software, R&D, Environmental Services and Conservation, Integrated Circuits and Autos.

The subsidies exist in various forms, including those directly affecting international trade such as:

(a) Export subsidies for FIEs and SOEs that meet certain export performance requirements. FIEs accounted for about 60 percent of China's exports of manufactured goods in 2005. The vast majority of FIEs that exported goods from China have corporate ties to countries neighboring China.

(b) Import-substitution subsidies that discourage purchases of foreign products by providing generous incentives for companies in China for buying domestic products rather than imports from the USA or other countries.

The Chinese central and provincial governments support both on-the-book and off-the book subsidies for domestic companies. Off-the book subsidies are far more pervasive and influential but also far more difficult to measure and to ascertain. Subsidies include:

1. **Free to Low-cost Loans**: The government exercises a vice-like grip on banks, stock markets and bond issuance and these translate to the ability to make grandiose loans. The most extreme statistics in the financial sector deal with loans outstanding. In three years from 2002 to 2004, loans increased by 58 percent, or $785 billion. In 2003, new lending equaled almost one quarter of gross domestic product (GDP). A credit binge fueled this latest boom. Half of all bank loans go to SOEs. Most of these loans will never be repaid. Huawei for example, has a $10 billion credit line from China Development Bank. Besides automatic roll-over of unpaid principal and interest, state-owned banks offers discounted lending rates to SOEs and domestic companies that satisfy certain export performance requirements . If the borrowers cannot pay back the subsidized loans, the banks convert the debt into equity in the SOEs or domestic companies.
2. **Asset Injections**: The SOEs' parent companies, usually municipal governments or ministries, provide their protégés with opportunities to acquire state-run businesses, such as toll bridges, at highly preferential terms which help pay down their costs. The governments also transfer ownership of shares and facilities between SOEs at below-market or no-cost levels. For example, in January 2005, Hubei province's government transferred at no cost a 51 percent stake in Ercheng Iron and Steel, a local steel producer with a production capacity of 3 million tons a year, to another state-owned producer, Wuhan Iron and Steel.
3. **No Break-even**: Poor book-keeping practices, and lax bottom-line considerations, grant SOEs freedom from the need to make profits, or to break even. "Pure state-controlled enterprises" have no disclosure requirements.
4. **Subsidized Purchases**: SOEs can purchase their components and raw materials below cost and directly from each other, affecting the competitiveness of certain sectors in the global economy. This tradition propelled the Chinese motorcycle industry's ability to buy control of virtually all Indian motorcycle companies short of Bajaj and turn them into assemblers of Chinese components.
5. **International Bargaining Power**: Beijing has used its enormous buying power to intercede for its SOEs with foreign suppliers and to reduce acquisition costs for raw materials. In 2006, the Chinese government attempted to influence negotiations between Chinese steel companies and global suppliers of iron ore by making clear that the government "would take necessary measures if prices were unacceptable and unreasonable". In 2005, China imposed export restrictions on coking coal, causing extensive disruptions in world markets and artificially lowering Chinese steel companies' manufacturing costs. The Chinese government has also secured contracts and exploration rights abroad for its SOEs.
6. **Labor Controls**: The government exercises various methods to control employees including the *dang'an* or employment dossier; and to reduce labor costs through injection of part-time and migrant workers and the use of prison labor. The government also offers exemptions from mandatory worker-benefit contributions to companies that satisfy certain export performance requirements
7. **Tax Breaks**: Many SOEs avoid taxation or reduce it through tax breaks (although this can backfire if a company's management loses favor). Income-tax reductions and refunds are available to companies that satisfy certain export performance requirements and that purchase Chinese-made equipment and accessories rather than imports
8. **Energy and Land Subsidies**: The state subsidizes gasoline and electricity. Currently, Beijing tightly controls the price of both gasoline and electricity at well below their true economic levels. The state also offers free land and utilities to SOEs and companies in key strategic sectors.
9. **Tariff and VAT Exemptions**: The state offers Value-added tax (VAT) and tariff exemptions to companies that satisfy certain export performance requirements. The state also offers VAT refunds to companies that purchase Chinese-made equipment and accessories rather than imports

10. **Sectoral Credit Allocation**: The Chinese economy speeds up or slows down on a sector-by-sector basis on credit allocations by Beijing. Some sectors such as automotive, steel, ethylene and metals' smelting have come off the boil. Others sectors such as coal, railways and utilities are still getting huge infusions of policy-mandated credit. Very high levels of bureaucratic interference characterize credit allocations and industrial-project approvals in China and the state banking system does not allow the market to price capital.
11. **Stock Listings**: SOEs and Collectives form over 93 percent of the listing of approximately 1200 companies on China's Shanghai and Shenzhen Stock Exchanges. Provincial governments pressure government regulators to discriminate against private companies and give the precious slots to their ailing state dinosaurs. Indeed, private companies without state connections cannot obtain a listing on any Chinese stock exchange
12. **Cheap Technology**: China runs a deficit on its technology trade with the rest of the world and FIEs control 80 percent of technological imports and exports in China. The Chinese have made little progress in either basic research or advanced design in vital industries. Despite this institutional flaw, SOEs such as Huawei owe much of their success to lax enforcement of laws governing the theft of intellectual property.
13. **Control over Distribution Channels**: Provincial and municipal governments control distribution channels to allocate and to manage market share, to protect favored industries from competition and to shape investment patterns. Regulations on distribution incorporate considerable ambiguities leading to both legitimate differences in interpretation and considerable legal efforts to find loopholes. Central and provincial governments routinely use this ambiguity to confer privileges on favored companies or industries, and to withhold normal rights from companies or industries as a form of protectionism. Local administrators have been known to seize goods being transported and to refuse transportation of goods through their jurisdictions. Administrative guidance from various and competing sources can override the basic laws or regulations either explicitly or unofficially. Provincial or municipal governments may interfere with the national limits on distribution by their generosity (to lure investment or to meet local goals) or restrictions (to protect local interests). *Guanxi* with local army officials assumes particular importance for distribution. Some estimates suggest that the PLA controls distribution of goods for up to about 80 percent of the Chinese population. Its control over manufacturing facilities also makes the PLA China's largest and most diversified manufacturer of industrial and consumer goods.
14. **Special Market Information**: Relevant information for strategic decisions comes at a premium price in China and often includes what we in the USA would consider Insider Information. In China, the central government deliberately controls and disseminates information that it considers of strategic importance. When restrictions on distribution insulate foreign or Chinese companies from their customers, they also cannot undertake direct market research and have to rely on less-sophisticated surrogates. For example, General Motors' (GMs') interns in Beijing have scoured the capital's streets to find out who is buying their cars after the intermediaries get them, so that GM can build *guanxi* with the buyers.
15. **Undervalued Currency**: The Chinese government's deliberate undervaluation of the yuan makes U.S. products more expensive for Chinese consumers who therefore purchase fewer of them. Conversely, China's undervalued currency also makes Chinese products cheaper in the USA, and therefore U.S. consumers purchase more of them, contributing to the record-high and still-growing U.S. trade deficit. The undervalued Chinese currency harms U.S. competitiveness and encourages the relocation of U.S. manufacturing overseas while discouraging investments in U.S. exporting industries. By some estimates, China's continued linkage of the yuan to the U.S. dollar provides Chinese steel exports with subsidies of 27–40 percent and imposes an effective, parallel tax on steel imports.

Monitoring Subsidies in China

Lack of transparency hinders ability to monitor all forms of subsidy except perhaps Stock Listings. Opacity serves as a tax which

1. Reduces ability to determine the true efficiency and productivity of China's labor and results in potentially sub-optimal foreign direct investment (FDI)

decisions until after commitments are made. Consequently, our research has shown that FDI enjoys higher ROIs and ROEs across entire industrial sectors in India against China, including Capital Goods; Food Beverage and Tobacco; Materials; Pharmaceuticals and Biotech; and, Software and Services.

2. Reduces the ability of U.S. domestic producers to prove dumping, especially as so many of those affected are Small and Medium-sized Enterprises with limited resources.
3. Magnifies the weakness of China's statistical system which depends too much on reporting and too little on sampling; the statistical system shows a systematic bias to over-report growth at the bottom of the economic cycle and under-report it at the top, i.e. to flatten out a much more volatile economic cycle. Recently, some foreign companies have started constructing their own physical-activity indices of everything from freight-barge traffic to power consumption and air miles flown to find true economic indicators, but the enormous expense constrains companies from doing this well.
4. Reduces the credibility of the SOEs' books. In 2006, according to SASAC, total revenues for the top 159 SOEs rose 20.1 percent to 8.14 trillion yuan and profits rose 18.2 percent to 755 billion yuan. These SOEs' net assets were worth 5.35 trillion yuan on total assets of 12.3 trillion yuan. Yet, SOEs may keep up to four sets of accounting books—for internal records, for the government, for foreigners and to know what is really going on.

Unreliability in macroeconomic data also seriously compounds the problem of estimating the effects of subsidies.

- For example, in February 2002, the Chinese government said that China's GDP had grown by 7.3 percent in 2001, making it the world's fastest-growing economy. However, only one province, Yunnan, reported that its product had grown slower than the national rate. Taken together, the provincial figures produced a national growth rate nearly two points higher than the official rate! The National Statistics Bureau (NSB) conducts sample surveys and uses these to estimate national GDP and growth rate. The results have invariably disagreed with provincial figures. In 1995, the GDP growth rate suggested by provincial data averaged three percentage points higher than the figure of 10.5 percent produced by sample surveys. Opinions vary about the accuracy of the central government's estimates. However, in China, few scholars publicly attempt any detailed justification of alternative figures because of political sensitivity.
- China's NSB also lacks the capacity to collect data outside normal information channels and lower-level officials interfere with its surveys. The numbers generated by provincial governments remain an important criterion in evaluating local officials' performance, creating an incentive for statistical falsification. The pressure to exaggerate statistics grew in the late 1990s as Chinese officials sought to pump up the economy to stave off the Asian economic slump's effects. Beijing declared that the country had to grow at least 7 percent a year to create jobs and to forestall social unrest. Not surprisingly, reported growth rates have not dipped below that level since.
- Officials may also routinely underreport other sensitive data such as debt numbers, unemployment or even FDI to avoid tax payments and governmental scrutiny. The central government's methods of ascertaining the validity of data, a process it calls *yasuo shuifen* or "squeezing the water," involves sample surveys, price-index adjustments and plenty of guesswork.
- Technical difficulties, such as staff reductions among statistical analysts, have enhanced errors in data. No comprehensive measures exist for the size of the fast-growing private-business and service sectors or even for what constitutes FDI.
- The Chinese government strictly controls economic and industrial data and even classifies some as state secrets. Routinely, Beijing has overvalued SOEs' stocks of unsold goods, and underestimated inflation. Other provinces underreport growth and activity: for example, Zhegiang province in Eastern China may have underreported growth to conceal the rapid development of private companies in its economy. Affluent provinces, such as Guangdong in Southern China, may also have underreported growth to avoid paying more taxes to the central government. However, without more systematic data, economists cannot definitively state if these factors pushed up growth or even if growth occurred.
- Governmental officials downplay unemployment figures to mask the suffering that economic reforms and restructuring have caused. The official unemployment rate of 3.6 percent in 2001 excluded *xiagang* workers (laborers receiving

small, monthly stipends from former companies and not counted as unemployed) that economists estimate to number about 10 million. The official rate also excluded farmers who left their fields to work in cities, a floating population of around 150 million unemployed migrants. Using international standards, China's unemployment rate in 2001 approximated 7.6 percent in rural areas and more than 8.5 percent in the cities, well above Beijing's red-flagged figure to indicate inevitable social turmoil.

- The central government's debt numbers look highly erroneous. The Central Bank's governor, Dai Xianlong, confessed to Parliament in April 2002 that national domestic debt appeared much higher than the official numbers (16 percent of GDP) suggested. Dai said debt appeared closer to 60 percent of GDP if one considered unfunded state-pensions' liabilities, local governments' debts, and major banks' nonperforming loans (NPLs). Dai's unusual candor may mask more bad news. Independent economists have discovered that Dai's statistics drew on China's yearbook GDP growth statistics. Debt more realistically appears closer to 100 or 125 percent of GDP. The Bank of China reported two different figures for its NPLs in 1999, one using Chinese accounting standards, another Western; the latter looms 2.6 times greater than the former. Moody's has openly called the books of China's "Big Four" banks, "meaningless."

Subsidies for the 11th Five-Year Program Period

I anticipate that all the subsidies that I identified will continue. The 11th 5-year plan specifically identifies certain strategically important industries that will receive state subsidies. These include:

1. Integrated circuits and software including technology for 90-nanometer and smaller integrated circuits
2. New-generation networks including digital TV networks and mobile communication
3. Advanced computing including technology for petaflop computer systems
4. Biomedicine including commercial production of vaccines
5. Civil airplane including general purpose planes and helicopters
6. Satellite applications including meteorological, oceanographic, navigation positioning and telecommunication satellites
7. New materials including high-performance materials in information biological and aerospace industries

Researchers may have more difficulties monitoring the rate of subsidization as China's 11th Five-Year Plan has only two numeric targets: per capita GDP in 2010 must be double the 2000 figure and "each work unit must cut its use of energy by 20 percent of current levels by 2010." The plan fails to mention raising the price of electricity and gasoline, and unlike the previous ten years, sets no economic growth targets.

Governmental Policies behind Subsidies

Our research has shown that despite recent deregulation efforts, state consumption through its SOEs dominates the Chinese economy. Subsidies permeate SOEs and well-connected private companies but do not extend to the bulk of private companies.

The subsidies appear huge. According to a World Bank study, 51 percent of all SOEs are losing money. Average current assets had risen to 319 days of annual sales, suggesting that most of the SOEs' assets lay in uncollectible bills or unsaleable inventory. In short, most SOEs were illiquid and massive injections of government money kept them alive.

The state offers subsidies to specific sectors and across sectors. Generally, SOEs and well-connected private companies with strong government network connections can access subsidies. The state is more likely to offer subsidies to private companies that promote strategic development efforts. The 11th Five-Year Plan identifies the following foci for development:

1. Advanced computing
2. Internet
3. Programming
4. Environmental services & resource conservation
5. Energy production and reserves
6. Value-chain positioning of Chinese manufacturing
7. Space, satellite and space-launch related capabilities

The state grants subsidies to companies that export, as well as to those that serve the domestic markets. Political rather than primarily economic considerations guide policies on subsidies. For example, many provincial governments offer subsidies as rewards to those that successfully manipulate government and business networks.

SOE reforms and strategic goals also shape policies on subsidies. However, for China's leadership, SOE reforms do not include concerns about profits or privatization. The reforms do not have as their goal reducing the state's control over key sectors of the economy, but rather making that control more effective. Consequently, the policies aim to make SOEs efficient and big enough to have a strong international presence such as the FIEs do. Specifically, the Chinese government wants its own global stars. The SASAC, which oversees SOEs, has the mandate to transform 30–50 SOEs into globally competitive national champions by 2010. These include PetroChina, ChinaMobile, Sinopec, CNOOC, Baosteel, China Aluminum, Shanghai Auto, Lenovo, TCL, and Quingdao Haier. Korea's chaebol, rather than Japan's keiretsu provides the guiding model for China's policy on industrial subsidies: through subsidies, the state helps the national champions to diversify their range of businesses and to link more closely to the state.

Some of the policies on subsidies stem from long and mid-range strategic plans; others derive from emergent planning and mistakes. For example, responding to the massive NPLs accumulated by Chinese banks in the 1990s, the government ordered they reduce their NPL ratios—bad loans as a proportion of total loans. However, this policy had unintended consequences. China's banks are technically insolvent but enjoy high liquidity. To cut NPL ratios, the banks merely increased the denominator of the ratios: their loans. Lending rose rapidly, driving growth as a side effect as NPL ratios fell from 28 percent in 2002 to 13.2 percent at the end of 2004. Assisting the process were transfers of old NPLs, made before the recent credit drive, to newly minted asset management companies (AMCs). The largest banks shifted an initial $169 billion in 1999–2000 and another $50 billion in 2005. The AMCs have become dumping grounds not just for commercial banks' NPLs but also for the assets of failed investment conglomerates, securities businesses and government-infrastructure projects. The state makes the AMCs issue interest-bearing bonds for which it refuses to accept explicit liability. Separately, Beijing has raided tens of billions of dollars of foreign exchange reserves to shore up banks' capital.

Policies regarding subsidies become difficult to unravel as the Chinese state encompasses central and local governments, with competing and often conflicting agendas, and different bureaucratic and political factions at the national level. Subsidies and the policies behind them reflect this fragmentation and conflict. Thousands of warring units that cohabit under the umbrella of the Chinese state control the SOEs. Consequently, SOEs enjoy direct subsidies stemming from state directives and elicit varying degrees of support.

AVIC, the national aerospace group, provides a good example of subsidies to an SOE serving a domestic market. Urged by Deng Xiaoping in 1985, AVIC had designed a civil airliner from scratch in less than 5 years. However, it only built two planes and even China's nationalized airlines refused to buy them. Two decades later, AVIC has received several tax breaks to build a small regional jet but has no idea of its commercial prospects.

Generally, despite stated policies, outsiders cannot ascertain the true policies that underlie subsidies. A secretive and authoritarian organization with unclear aims, closed to scrutiny and debate, controls the Chinese state. More effectively placed subsidies appear in the SOEs that the Beijing central government has classified as global champions. However, recent examples illustrate their complexity. CNOOC, whose $19 billion bid for Unocal touched off volcanic reactions, is a Hong Kong-listed firm 70 percent owned by an unlisted parent company, all of whose shares are owned by the central government agency, SASAC. Beijing has helped CNOOC to acquire contracts to control foreign-energy reserves and the company heavily relies on subsidized finance from SASAC. Local governments control other SOEs. These include white goods maker Haier (owned by the Qingdao city government), which launched an unsuccessful bid for Maytag, and the municipally owned Shanghai and Nanjing car companies that have spent the last several months picking through MG Rover. These companies also receive subsidies in line with Beijing's stated goals of creating state-owned multinationals and retaining domestic control over key sectors, such as car making. The demands of both the central government, which sets industry policy, and their local government overlords, whose interests may conflict with Beijing's industrial-policy goals, shape the subsidies the SOEs receive, as well as the SOEs' evolution, strategies and policies. Huawei, a maker of telecoms-network equipment, illustrates a third level of policies and subsidies. Huawei is ostensibly privately owned, although many of its shares are owned by the local state telecom authorities to whom it has sold equipment. It enjoys a $10 billion low-interest credit line from the China Development Bank, whose mission is to make concessional loans in support of the state's policy goals. Huawei also has strong ties to China's military.

Market Distortions and Profitability of FIEs in China

The large numbers of Chinese subsidies targeted towards drawing FDI (see Table 1) have not enhanced FIEs' profits, indicating market distortions, misallocation of funds and excess capacities. Few FIEs disclose their Chinese operations' real performance, and estimates have relied on business surveys and anecdotes. Our research reveals that only about one-third of the FIEs operating in China have ever made a profit there, and profits have been concentrated in the hands of a few companies. In addition, historically, foreign affiliates in China have lower profit margins than their global average.

Despite some profitable FIEs, trends on profits have not changed substantially since China's entry into the WTO. For example, in 1998, a survey of 229 FIEs by management consultants A. T. Kearney showed that only 38 percent of all manufacturers were covering their operating costs. If the companies had included their borrowing costs, or costs of capital, fewer still could have claimed to have broken even.

Another study done at the Chinese Academy of International Trade and Economic Cooperation showed that about one-third of the 354,000 foreign companies operating in China in 2001 turned a profit. Yet, a 1999 survey by the American Chamber of Commerce in China showed that, while 58 percent of its member companies had lower profit margins there than in other global operations, 88 percent had plans to expand. Deloitte & Touche's survey in 2002 confirmed that 90 percent of FIEs in China planned to expand their operations within the next three years. In 2003, about 424,196 FIEs, big and small, operated in China (MOFTEC). Michael Furst, Executive Director of the American Chamber of Commerce, Beijing, informed us that about two-thirds of its member companies were making some profits but not up to anticipated levels, while about one-third were making losses. These figures correspond to those from 2004.

A 2004 survey by China Economic Quarterly shows that the earnings of U.S. affiliates in China, which includes the affiliates' profits, and earnings booked through Hong Kong and Singapore, rose to $4.4 billion. When all other sources of profit are added—including royalty and licensing fees and income from private services—these affiliates earned $8.2 billion in 2004. However, U.S. companies made $7.1 billion in Australia, a market of only 19 million. They earned $8.9 billion in Taiwan and South Korea, emerging economies with a combined population of 70 million, and earned $14.3 billion in Mexico. Most respondents could not achieve profit margins above their global average.

A large proportion of the earnings end up with a small number of FIEs that enjoy lucky breaks in China's heavily regulated operating environment. For example, Mobile Telecommunications encountered no vested interests in China and contributed about half of the U.S. companies' mainland-reported earnings as recently as 2001. However, from 2002, Chinese companies, subsidized by the state, moved into mobile handsets and their cutthroat pricing destroyed profits in that sector.

More recently, a consumer loan boom financed by state-run banks underwrote an explosion in car sales that dropped later like a brick—but Volkswagen, the market leader, still earned $1.2 billion in China in 2003.

Five U.S. companies, including three car makers, accounted for one third of equity profits that mainland affiliates reported. General Motors alone booked $437 million in earnings. Fast-food companies Yum Brands—owner of KFC—and McDonald's topped off the list. Fast-food companies have consistently made profits in the Chinese domestic economy. They face no competition from state interests and, as services, are less prone to intellectual property abuses. Yum Brands, which has 1,200 restaurants in China, and McDonald's, probably earned about $200 million and the U.S. car companies in excess of $500 million—equivalent to about one-third of mainland equity income of $2.4 billion. These figures underline how small China's domestic markets may be.

The exaggerated economic data can have significant effects on perceived performance and projected performance of FDI in China. The successful companies in our research did not rely on economic and industrial data. As Elmar Stachels, Managing Director of Bayer China Company, Ltd., told us, "You manage by objectives, objectives that must be clearly stated—then determine what kind of tools you can use to determine if you achieved them, but stick with your objectives. However, if it comes to financial figures, it will be challenging. What good will numbers be if the base rates used for comparison of performance are not reliable."

China remains embroiled in overcapacity and excess production as state investment and subsidies move across sectors, and companies' profits correspondingly whipsaw. A year ago in the auto sector, sales growth for many car models dropped from three digits to less than zero in a few months. In steel, China flipped from a massive net importer to a net exporter in less than a year. In the past nine months, the global price of ethylene—a base constituent of plastics—dropped by half as Chinese production capacity expanded 35 percent this year and will probably double in the next few years. Soon, smelted copper will join the ranks: China has 2.5 million tons of annual production capacity and another 2.5 million tons under construction. Similarly, in stainless steel, China's annual production capacity approximated 2.5 million tons at the end of 2004. Industrial projects and subsidies will expand this to 10 million tons in five years.

CVDs and China

For more than two decades the U.S. Department of Commerce ("Commerce") has refused to apply the CVD law to unfairly subsidized and injurious imports from nonmarket economies such as China. Commerce has argued that pervasive governmental intervention hinders meaningful comparisons between subsidized and market-determined prices.

Measurement issues also arise as China's opaque environment obstructs the identification of appropriate benchmarks. For example, China's financial system provides many subsidies. However, governmental control over banking obfuscates market-determined rates of interest that can provide benchmarks to gauge credit subsidies' benefits for companies or industries. Also, lack of adherence to generally recognized accounting standards and unreliable book-keeping further complicate our identifying subsidies' benefits. Yet, China's WTO accession agreement specifically permits application of third-country information in CVD determination and encourages requests for valid information from the Chinese government to understand subsidies.

Approximate CVD rates may grossly underestimate the amounts required to offset China's pervasive subsidies. For example, a Chinese company may receive governmental credit subsidies that reduce its capital costs by 20 percent. This advantage may dramatically enhance the company's ability to compete in international markets. However, Commerce calculates CVD rates by dividing the total value of the subsidies' benefits by the total value of the exporting companies' sales. Since the subsidy in our example affects only one portion of the company's balance sheet (capital costs), the CVD applied to offset this benefit may fall below 20 percent. The company may also amortize loans and other non-recurring benefits, such as equity infusions, over several years, further reducing the CVD rate.

Despite these limitations, when dealing with China and other nonmarket economies, CVDs, as proposed by the *Nonmarket Economy Trade Remedy Act of 2007* offer more cost-effective, though less efficient, solutions for offsetting subsidies than anti-dumping provisions do. The CVDs represent the classic case of preferring half a loaf to no bread. The CVD rates to offset Chinese subsidies prescribed will probably fall far short of the actual subsidies. However, they do offer partial remedies to offset market distortions and inefficient allocation of resources by the Chinese government. Making CVDs available against China would give U.S. companies an explicit import-relief measure that targets unfair government subsidies. CVDs are also more accessible to Small and Medium-sized Enterprises in the USA that cannot afford to undertake anti-dumping litigation and so would provide one small step in our efforts to level the global playing field.

Thank you again for providing me with this opportunity to present some of my research on subsidies in China, market-distortion effects on competitive environments and remedies offered by CVDs.

Table 1. China's Subsidy Notification to WTO in 2006

Primary Beneficiary of Subsidies	Total No. of Subsidy Programs	Subsidy Program ID
Foreign Invested Enterprises/Foreign Equity Joint Ventures	14	1, 2, 3, 4, 5, 6, 7, 8, 10, 11, 12, 13, 27, 58
Agriculture/Animal Husbandry	14	29, 36, 37, 38 39, 40, 41, 42, 46, 47, 48, 49, 50, 66
Forestry/Grassland Rebuilding	7	30, 51, 52, 53, 54, 55, 56
Welfare/Disability/Unemployment Relief	5	21, 24, 63, 72, 73
Poverty Relief	4	15, 16, 17, 18
Disaster Relief	4	20, 43, 44, 45
Technology Training/Acquisition	4	28, 31, 59, 60
Promotion of Research Institutes	3	25, 26, 71

Table 1. China's Subsidy Notification to WTO in 2006—Continued

Primary Beneficiary of Subsidies	Total No. of Subsidy Programs	Subsidy Program ID
Environmentally Friendly Production/ Waste Management	3	19, 69, 70
Promotion of Small and Medium Sized Enterprise	3	32, 33, 34
Food Security	2	61, 62
Wildlife Conservation	2	67, 68
Training of Migrant Rural Labor	1	35
Support of Low Profit Enterprises	1	22
Support for Township Owned State Enterprises	1	23
Poppy Eradication	1	65
HIV/AIDS Relief	1	74
Western Regional Development	1	14
Support for Hi Tech/Industrial Economic Zones	1	9
Promotion of Specific Industries:		
Integrated-Circuit	1	57
Tea	1	64
Copper-Refining	1	75
Casting/Forging	1	76
Dies	1	77
Machine-Tool	1	78

Chairman LEVIN. Thank you very much.
Mr. Porter.

STATEMENT OF DANIEL L. PORTER, PARTNER, INTERNATIONAL TRADE GROUP, VINSON & ELKINS LLP

Mr. PORTER. Good afternoon.

My name is Daniel Porter. I'm a partner in the law firm of Vinson & Elkins, specializing in international trade.

I appear today solely in my personal capacity. I am not appearing on behalf of the Chinese government or any other client.

Rather, I am here in response to a request from the Subcommittee to share my personal thoughts about the bill, H.R. 1229.

Mr. Chairman, I appreciate this invitation and the opportunity to discuss these issues with you.

My remarks today will be a brief summary of my written statement that was provided to the Committee yesterday.

At the outset, I note that it is not my position that the U.S. Congress should not pass legislation authorizing the application of the U.S. countervailing duty law to nonmarket economies such as China.

I fully recognize the ability and right of the United States to make amendments to its trade remedy laws to ensure that imports are fairly traded.

That stated, I also believe that any changes to the U.S. trade remedy laws should be fair and not impose unreasonable or unwarranted restrictions on imported products.

Like others, I see a few problems with the bill as currently drafted.

The first problem is that the bill requires congressional approval before a country can graduate from nonmarket economy status to market economy status.

If enacted, such legislation would represent the only instance in which Congress would become involved in the day-to-day application of the Antidumping Duty (AD) and CVD laws. With all due respect, this is not the role of Congress.

Rather, like other aspects of the AD and CVD laws, Congress should establish the criteria it wants to be applied and then instruct the responsible agency to implement that criteria.

This is particularly true in the anti-dumping world, given that anti-dumping duties are assessed on a retrospective basis and all interested parties are permitted to appeal a Commerce Department final determination to the Court of International Trade.

I respectfully submit that Congress should not be involved in the day-to-day application of trade remedy laws to individual cases.

The second problem is that the current draft of the bill requires the Commerce Department to calculate the amount of benefit of the CVD rate by utilizing benchmarks outside China.

With all due respect, such provision is not needed, not fair, and contrary to the provisions of China's WTO accession protocol.

Mr. Chairman, such provision is not needed.

The underlying premise of this provision, that the alleged control of the economy by the Chinese government makes it impossible ever to utilize appropriate benchmarks from within China to calculate the subsidy benefit is simply at odds with the numerous factual findings concerning the real world of China today.

Over the past couple of years, there have been many studies demonstrating that the Chinese government has undertaken significant reforms to promote the introduction of market forces in the economy.

Such factual conclusions indicate that there are sectors in the economy that operate under market principles, and therefore could provide suitable benchmarks for measuring the extent of the subsidy benefit.

As importantly, requiring the Commerce Department to adopt such a presumption would be contrary to the provisions of China's WTO accession protocol.

The language of Article 15(b) makes clear that before utilizing surrogate benchmarks and CVD cases against China, the United States must first make a specific factual finding that there are special difficulties with utilizing benchmarks in China.

A requirement to find special difficulties necessarily implies that such finding be made on a case by case basis.

The reason is that every case is different. Different products have different producers and different industries operating in different sectors of the economy.

I submit that by not allowing the Commerce Department to make this finding on a case by case basis, the bill does not honor the United States' agreement made in China's WTO protocol.

The third problem with the current draft of the legislation is that it does not prevent double counting of duties—that is, imposing two sets of duties to compensate for the same unfair trade practice in those situations in which the same exporters face both an anti-dumping and somebody case.

The double counting problem stems from the special anti-dumping rules that are applied to nonmarket economies. Very simply, the special anti-dumping rules that are applied to nonmarket economies such as China already offset much subsidization.

Let me give you a quick example.

Assume that because of subsidies a Chinese steel producer is able to purchase iron ore more cheaply. Rather than having to pay the market price of $100 of iron ore the subsidies allow him to incur only an $80 cost.

However, the special anti-dumping rules that are applied to nonmarket economies take this into account.

Under existing law, when calculating anti-dumping margins for this company, the Commerce Department is required to use the $100 iron ore cost, not the producer's actual cost of $80. The use of the higher cost results in a higher anti-dumping margin.

To impose CVD duties on top of those AD duties would result in double counting.

The final problem of the bill is the effective date. H.R. 1229 states that the changes to the law shall apply to CVD petitions filed on or after October 1, 2006.

Use of such a date is an obvious attempt to make legal the ongoing CVD case on coated free sheet paper that was filed on October 31, 2006.

Mr. Chairman, such retroactive application of changes to the trade remedy laws is not fair to the Chinese government and Chinese exporters participating in the ongoing CVD case.

To apply H.R. 1229 retroactively is equivalent to punishing them for acts that were legal at the time they were committed.

It is for these reasons that retroactive legislation has always been looked upon with disfavor.

Mr. Chairman, in conclusion, I want to say there is a simple fix to all the problems that I have identified with H.R. 1229.

Change H.R. 1229 to reflect the language of Section 3 of H.R. 3283, the bill that authorized the application of the CVD law to nonmarket economies that was passed by the House in the 109th Congress.

H.R. 3283 accomplishes the overall objective of ensuring that there can be CVD cases against NME countries but does so in a manner that is fair and that honors the U.S. obligations in how it will apply the AD and CVD laws.

Mr. Chairman, that concludes my testimony. I appreciate the attention of the Committee, and would be happy to respond to any questions.

[The prepared statement of Mr. Porter follows:]

Prepared Statement of Daniel L. Porter, Partner, International Trade Group, Vinson and Elkins LLP

Good afternoon. My name is Daniel Porter. I am a partner in the law firm of Vinson & Elkins LLP specializing in international trade. I have represented clients in various trade remedy proceedings, including antidumping and countervailing duty cases, for more than 20 years. Currently, this work includes, among other projects, representing the Chinese Government in the Commerce Department's countervailing duty investigation on coated free sheet paper from China, and representing the Chinese Government, a Chinese exporter and a U.S. importer in a court case that seeks to stop this very Commerce Department CVD investigation.

I appear today solely in my personal capacity. I am not appearing on behalf of the Chinese government or any other client. Rather, I am here in response to a request from the Subcommittee to share my personal thoughts about H.R. 1229. I appreciate this invitation and the opportunity to discuss these issues with you.

At the outset I note that it is not my position that the U.S. Congress may not or should not pass legislation authorizing the application of the U.S. countervailing law to non-market economies such as China. I fully recognize the ability and right of the United States to make amendments to its trade remedy laws to ensure that imports are fairly traded.

That stated, I also believe that any changes to U.S. trade remedy laws should be fair and not impose unreasonable or unwarranted restrictions on imported products. Said differently, while I recognize and appreciate the desire for U.S. producers to have a level playing field, I do not think it is appropriate to change the law to tilt the field in ways unfair to U.S. importing interests. As currently drafted, I believe that H.R. 1229 does not satisfy the objective of achieving a level playing field, but rather tilts the field the other way.

I see four problems with H.R. 1229 as currently drafted.

Problem #1: Requiring Congressional Resolution of Approval Before Allowing Termination of NME Status

First, H.R. 1229 requires that any country designated a non-market economy retain that status until both the Commerce Department determines to revoke the non-market country designation and graduate the country to market economy status *and* Congress passes a joint resolution approving the Commerce Department's action.

If enacted, this legislation would represent the only instance in which Congress would become involved in the day-to-day application of trade remedy laws to individual cases. Rather, as it has done before, Congress should establish the criteria it wants to be applied and then instruct the responsible agency to implement the criteria. It makes no sense for Congress to act as some sort of reviewing body to determine whether the Commerce Department properly applied the criteria for graduating a country to market economy status.

This is particularly true in the antidumping world given that AD duties are assessed on a retrospective basis and all interested parties are permitted to appeal a Commerce Department's final determination to the Court of International Trade. Indeed, if this provision is passed, you very well could have an anomalous situation in which the Commerce Department decides to revoke the NME status of country, Congress subsequently passes a resolution approving the revocation, but then later the Court of International Trade rules that the Commerce Department original decision to revoke the NME status was not supported by substantial evidence on the record. Needless to say, this would be a rather awkward legal and procedural situation. I respectfully submit that Congress should not be involved in the day-to-day application of trade remedy laws to individual cases.

Problem #2: Requiring Third Country Benchmarks for Calculation of Benefit

The second problem is that the current draft of H.R. 1229 requires Commerce Department to calculate the amount of the benefit—the CVD rate—by utilizing benchmarks outside China. Essentially, as long as China continues to be designated a non-market economy country, under H.R. 1229 the Commerce Department is prohibited from ever using any benchmarks from China to calculate the subsidy benefit. With all due respect, such provision is not needed, is not fair, and is contrary to the provisions of China's WTO Accession Protocol.

First, the underlying premise of this provision—that the alleged control of the economy by the Chinese Government makes it impossible ever to utilize appropriate benchmarks from within China to calculate the subsidy benefit—is at odds with numerous factual findings concerning the real world economy of China today. I note that in its comprehensive examination of the Chinese economy published last August, the Commerce Department itself made the following factual observations:

> "The PRC Government has undertaken significant reforms to promote the introduction of market forces into the economy."
>
> "The Department notes that China permits all forms for foreign investment, e.g. joint ventures and wholly-owned enterprises, in most sectors of the economy. Foreign investors are free to repatriate profit and investments are protected from nationalization and expropriation."
>
> *See* Commerce Department decision memorandum, dated August 30, 2006, re: China's status as a non-market economy prepared for its antidumping inves-

tigation of *Certain Lined Paper Products from the People's Republic of China* at p. 3.

Such factual conclusions strongly suggest that, even if China as a whole does not meet the criteria for graduating to market economy status, there can be little question that there are sectors in the economy that operate under market principles and therefore could provide suitable benchmarks for measuring the extent of the subsidy benefit. There is simply no longer any basis to presume that suitable benchmarks can never be found in China.

As importantly, requiring the Commerce Department to adopt such a presumption would be contrary to the provisions of China's WTO Accession Protocol. Article 15 (b) of the protocol states that when calculating the benefit of subsidies the relevant provisions of the WTO SCM agreement shall apply; however, "*if there are special difficulties in that application,*" the importing WTO member may then use alternative methodologies to identify and measure the subsidy benefit.

It is clear from this language that the U.S. may resort to surrogate benchmarks only after making a specific factual finding that "there are special difficulties" with utilizing benchmarks in China. Or stated differently, a requirement to find special difficulties necessarily implies that such finding be made on a case-by-case basis. The reason is that every case is different—different products have different producers in different industries operating in different sectors of the economy. A finding that special difficulties exist in one sector does not mean that the same special difficulties will exist in another.

There is no question that China's WTO Protocol specifically allows the U.S. to utilize surrogate benchmarks in certain CVD cases when measuring subsidies. However, there is equally no question that in extracting this agreement from China, the U.S. promised that it would only resort to surrogate country benchmarks upon a factual finding of "special difficulties." H.R. 1229 requires the U.S. to renege on this specific promise.

There is a simple fix to this problem—change H.R. 1229 to reflect the language of Section 3 of H.R. 3283, a bill that authorized the application of the CVD law to NME countries that was passed by the House in the 109th Congress. The language of H.R. 3283 correctly reflected the agreement in the China WTO Protocol. If the Congress takes any action on this issue, I respectfully urge the re-adoption of H.R. 3283.

Problem #3: No Provision To Avoid Double Counting

The third problem with the current draft of the legislation is that it does not prevent double counting of duties—that is, imposing two sets of duties to compensate for the same unfair trade practice—in those situations in which the same exporters face *both* an antidumping and a CVD case.

The double counting problem stems from the special antidumping rules that are applied to non-market economies. Very simply, the special antidumping rules that are applied to NME countries such as China already offset most subsidization. Specifically, under the special NME methodology mandated by the existing AD law the Commerce Department does not use Chinese producer's actual costs. Rather the Commerce Department restates the Chinese producer's costs based on information from a surrogate market-economy. Most importantly, when the Commerce Department restates the Chinese producer's costs, by law, Commerce may *only* use surrogate values that are subsidy free.

To understand double counting, it is necessary to compare what happens in a market economy context with what happens in a non-market economy context when there are both antidumping duties and countervailing duties imposed on the same product.

I will use raw material inputs as an example. I will also use "constructed value" as an example, since the NME methodology is essentially a constructed value methodology which substitutes surrogate values or imported value inputs for actual input values. We can thus easily and directly compare to different rules for a market economy and non-market economy context.

In a market economy context, Commerce bases constructed value on the foreign producer's *actual costs* of the raw material inputs, whether or not that input is subsidized. Thus, for example, assume that the major input is iron ore and its market value is 100 per ton. However, let's assume that the government in the exporting market economy country provides a subsidy of 20 for purchases of iron ore and, therefore, the export producer in fact only pays 80 for the iron ore.

For the dumping calculation in the market economy case, the actual cost to export producer would be used—the raw material costs of 80. For the subsidy calculation, the subsidy amount of 20 would be used. Therefore, to the extent that constructed value and dumping margins are lowered by 20 because of the subsidized input, this lower cost would be captured by virtue of the countervailing duty imposed to offset the subsidy of 20 received by the producer. In market economy cases the two laws work in tandem, in a logical and consistent manner.

The same facts in an non-market economy (NME) context, however, yield a very different result. The raw material inputs in an NME context are *not* valued based on the cost to exporter/producer, but are based either on a market economy surrogate value or the arm's length purchase price of the raw material imported from a market economy. Under either method, the Commerce Department is prohibited from using any values that reflect subsidies. Thus, in an NME case, Commerce would use the actual value of 100 in the above example, *not* the actual subsidized cost paid by the company. The fact that the Chinese exporter/producer may be receiving a subsidy of 20 on its raw material becomes irrelevant because by valuing the raw material at 100 the effects of the subsidized input are already fully offset. Thus, to use 100 in constructing normal value in the NME context and then adding a subsidy of 20 would essentially double count the benefit of the subsidy to the NME exporter/producer.

I note that the conclusion that the application of current AD and CVD laws to NME countries (as contemplated by H.R. 1229) would result in unfair double counting is not just my conclusion. The United States Government Accountability Office (GAO) reached the same conclusion based on its analysis of applicable laws and discussions with Commerce officials. Indeed, the GAO report noted that (a) Commerce officials admitted that if both CVD and antidumping duties are applied to NME countries they would have no authority, under existing law, to avoid double counting and (b) two U.S. courts have suggested that double counting to compensate for the same unfair trade practice is generally considered improper." *See* U.S. Gov't Accountability Office, GAO–05–474, *U.S.-China Trade: Commerce Faces Practical and Legal Challenges in Applying Countervailing Duties* (June 2005) at pp. 27–28, and U.S. Gov't Accountability Office, GAO–06–608T, *Testimony Before the U.S. China Economic and Security Review Commission* (April 4, 2006) at p. 18.

As importantly, significant U.S. companies also have expressed their concern about the unfairness of double-counting AD and CVD duties. For example, General Motors submitted the following statement in response to the Commerce Department's request for comments on whether the CVD law should be applied to non-market economies:

> General Motors takes the position that the use of anti-dumping and countervailing duty law and the methodologies used to identify and address unfair trading practices must be fair and balanced.
>
> With regard to the specific issue of non-market economies, any advantage gained by such economies because of the reluctance of the U.S. to pursue subsidy cases has clearly been offset by the disadvantage that non-market economies experience in antidumping cases. Since World Trade Organization rules allow the use of factors of production analysis as a proxy for prices in non-market economies, designation as a non-market economy represents a significant penalty in anti-dumping proceedings, particularly in the U.S. where factors of production analysis is routinely used.
>
> Given this situation, we believe that industries should be treated consistently in both countervailing duty and anti-dumping proceedings.
>
> *See* General Motors letter dated January 12, 2007 to Susan Kuhbach, Senior Office Director for Import Administration, U.S. Department of Commerce.

I agree with the General Motors. It is essential that any legislation that authorizes the Commerce Department to apply CVD duties to non-market economy countries must take into account the special antidumping rules that are applied.

Again, it is easy to fix this problem—change H.R. 1229 to reflect the language of Section 3 of H.R. 3283, a bill that authorized the application of the CVD law to NME countries that was passed by the House in the 109th Congress. The language of H.R. 3283 simply stated that the Commerce Department shall ensure that any countervailing duties that are applied to a non-market economy country are not double-counted in an antidumping case against the same products. This is the correct approach. Again, if Congress takes any action, I respectfully urge the re-adoption of this language of H.R. 3283.

Problem # 4: Unfair Retroactive Application

The final problem of H.R. 1229 is the effective date. H.R. 1229 states that the changes to the law shall apply to CVD petitions filed on or after October 1, 2006. Use of such date is an obvious attempt to make legal the ongoing CVD case on coated free sheet paper that was filed on October 31, 2006.

Mr. Chairman, such retroactive application of changes to the trade remedy laws is not fair. Supreme Court precedent make clear that retroactive application of statutes is highly frowned upon given the constitution's prohibition against *ex post facto* laws and bills of attainder. Moreover, the idea of retroactive application is just unfair. Through this effective date provision, Congress is unfairly targeting the Chinese lined-paper case and, with it, the respondents in the investigation. These respondents had relied upon the consistently applied 23 year interpretation that the current CVD law does not apply NME countries. To apply H.R. 1229 retroactively is equivalent to punishing them for acts that were legal at the time they were committed. It is for these reasons that retroactive legislation has always been looked upon with disfavor.

Mr. Chairman, I urge you to correct this deficiency. As before, the fix can be found the language of H.R. 3283. H.R. 3282 would have applied only to new CVD petitions that were filed 30 days after the date the legislation became law.

This concludes my testimony. I thank you for your attention. I would be happy to answer any questions.

Chairman LEVIN. Thank you very much.

Mr. Hecht.

STATEMENT OF JAMES C. HECHT, PARTNER, INTERNATIONAL TRADE PRACTICE, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP

Dr. HECHT. Thank you. Good afternoon.

I am Jim Hecht, and I practice in the international trade area at the law firm of Skadden, Arps, Slate, Meagher & Flom.

The views I will provide today are my own and not necessarily those of the firm.

I appreciate the opportunity to provide a few comments on H.R. 1229 and would of course be happy to answer any questions you might have.

The issue of subsidies in nonmarket economy countries, and in particular China, has become a major focus in the trade policy area for some time now.

In the past, debate on application of CVD law to NMEs has focused on whether subsidies can be meaningfully isolated in such economies. Recent events would appear to resolve that issue.

In this regard, the Administration has repeatedly expressed strong concern at the evidence of significant subsidization in China impacting a range of industries.

In acceding to the WTO, China specifically committed itself to abide by WTO subsidy disciplines and to eliminate prohibited subsidies.

As part of its WTO obligations, China has identified and notified scores of subsidy program that continue to provide benefits to Chinese industries.

The United States has recently requested consultations under the WTO dispute settlement system, with regard to nine prohibited subsidy programs in China.

In light of these facts, there can be little doubt that subsidies in nonmarket economies can be and have been specifically isolated and identified, as shown by the recent actions of both the United States and Chinese governments, and as such, there would appear to be no valid legal or policy reason why U.S. trade disciplines in the subsidy area should not apply to nonmarket economies just as they do with respect to market economies.

In fact, there are already clear grounds under existing law to apply U.S. countervailing duty provisions to nonmarket economies, and in this regard, the Administration is currently considering whether to modify its longstanding policy of not applying CVD rules to such economies.

Notwithstanding the possibility of a change in the regulatory practice, however, there are good reasons for legislative action to clarify the issue.

Legislation such as H.R. 1229 would remove legal uncertainty in the area, would obviate the possibility of future regulatory changes of policy, and would allow Congress to address the manner in which CVD law will be applied to nonmarket economies.

One methodological issue that has been raised is the relationship between the CVD law and the nonmarket economy methodology used in anti-dumping cases, and specifically whether additional legislative action may be necessary to prevent a double assessment of duties for so-called domestic subsidies.

In prior comments on the topic, the Administration has taken the position that requiring such an adjustment is neither warranted nor appropriate. In my view, that position is correct.

Even aside from the obvious administrative difficulties in trying to undertake an additional analysis in this area, the theoretical concern that has been expressed with regard to double counting is not well founded.

Specifically, it is not correct to say that the nonmarket economy dumping methodology corrects for domestic subsidies.

Rather, it corrects for price distortions that result in both artificially high and artificially low input prices in a nonmarket economy.

As such, there is no basis to conclude that domestic subsidies will be remedied through the NME dumping methodology.

H.R. 1229 would also make a change in current law to require that Congress approve any graduation of a country from nonmarket to market economy status.

Nonmarket economy treatment can be critical to the operation of U.S. trade laws, particularly where the lack of reliable price and cost data in a nonmarket economy makes application of traditional market economy rules inadequate.

Under current law, graduation decisions are made unilaterally by the Administration.

Given the importance of NME graduation decisions to U.S. industries and to the U.S. economy, as well as the concerns that have been expressed in the past by Members of Congress with respect to such decisions, allowing Congress to weigh in before the fact would make a great deal of sense.

Again, I appreciate the opportunity to be here and would be happy to answer questions.

[The prepared statement of Mr. Hecht follows:]

Prepared Statement of James C. Hecht, Partner, International Trade Practice, Skadden, Arps, Slate, Meagher and Flom LLP

Good afternoon. I am Jim Hecht, and I practice in the international trade area at the law firm of Skadden, Arps, Slate, Meagher and Flom. The views I will provide today are my own and not necessarily those of the firm.

I appreciate the opportunity to provide a few comments on H.R. 1229, the "Non-market Economy Trade Remedy Act of 2007" and would of course be happy to answer any questions.

The issue of subsidies in non-market economy countries—and in particular China—has been a major focus in the trade policy area for some time, as well as a matter of urgency for a number of potentially impacted U.S. industries. In this regard,

- The Administration has repeatedly expressed strong concern at evidence of significant subsidization in China, impacting a range of industries.
- In acceding to the WTO, China specifically committed itself to abide by WTO subsidies disciplines and to eliminate prohibited subsidies.
- As part of its WTO obligations, China has identified and notified scores of subsidy programs that continue to provide benefits to Chinese industries.
- The U.S. has recently requested consultations under the WTO dispute settlement system with regard to 9 prohibited subsidies programs in China.

In light of these facts, there can be little doubt that subsidies in non-market economies can be, and have been, specifically isolated and identified—as shown by the recent actions of both the U.S. and Chinese governments. And as such, there would appear to be no valid legal or policy reason why U.S. trade disciplines in the subsidies area should not apply to non-market economies—just as they do with respect to market economies.

In fact, there are already clear grounds under existing law to apply U.S. countervailing duty provisions to non-market economies. And in this regard, the Administration is currently considering whether to modify its longstanding practice of not applying CVD rules in the context of such economies.

Notwithstanding the possibility of a change in regulatory practice, however, there are good reasons for legislative action to clarify the issue. Legislation such as H.R. 1229 would remove legal uncertainty in this area, would obviate the possibility of future regulatory changes of policy, and would allow Congress to address the manner in which CVD law will be applied to non-market economies.

One methodological issue that has been raised is the relationship between the CVD law and the non-market economy methodology used in anti-dumping cases—and specifically whether additional legislative action may be necessary to prevent a double assessment of duties for so-called "domestic" subsidies. In prior comments on the topic, the Administration has taken the position that such an adjustment is neither warranted or appropriate. In my view, that position is correct. Even aside from the obvious administrative difficulties in trying to undertake an additional analysis in this area, the theoretical concern that has been expressed with regard to double counting is not well-founded. Specifically, it is not correct to say that the non-market economy dumping methodology corrects for domestic subsidies—rather, it corrects for price distortions that result in *both* artificially high and low input prices in a non-market economy. As such, there is no basis to conclude that domestic subsidies will be remedied through the NME dumping methodology.

H.R. 1229 would also make a change in current law to require that Congress approve any graduation of a country from non-market to market economy status. Non-market economy treatment can be critical to the operation of U.S. trade laws, particularly where the lack of reliable price and cost data in a non-market economy makes application of traditional market economy rules inadequate. Under current law, graduation decisions are made unilaterally by the Administration, with no opportunity for judicial review. Given the importance of NME graduation decisions to U.S. industries and the U.S. economy—as well as the concerns that have been expressed in the past by Members of Congress with respect to such decisions—allowing Congress to weigh in before the fact would make a great deal of sense.

Again, I appreciate the opportunity to be here and would be happy to answer questions.

Chairman LEVIN. Thank you very much, and to all of you.

Mr. Herger.

Mr. HERGER. Thank you, Mr. Chairman.

I believe just about everyone recognizes that we have a major problem with China.

We have a major problem in that we're dealing with this huge nation that's growing so rapidly, and is coming from a point where it did not have a free enterprise system, and we have problems there.

My concern is that when we do what we do in correcting these problems, we not do it in a way that we lose when we get into a settlement fight with them in the WTO and end up penalizing even more some of our U.S. companies.

So, with that in mind, Mr. Phelps, in your testimony, you say that the H.R. 1229 will make industries in other countries more competitive rather than the American industry.

Could you elaborate on how other countries would benefit?

Mr. PHELPS. Thank you, Congressman.

Yes.

CITAC's general view is, particularly in the United States, where we must, and steel industry people can debate this endlessly, we must import 20 percent, 25 percent, whatever the number is, of our steel every year, because the industry simply doesn't make enough steel, or you could say the consuming sector is so vibrant in the United States that we need more steel than is made.

It is absolutely crucial for those companies, whether they're a small metal bender, a parts manufacturing operation, integrated with one of the big three auto companies, that they have to be able to get their material at prices that are internationally competitive.

Without that, they are themselves put at risk for imports of their products.

Our concern is, when the U.S. prices are artificially posted higher, that the metal benders and the parts makers and the people who are supplying fenders to GM, Ford, and Chrysler and others, simply are going to lose their business to offshore suppliers of those products.

Mr. HERGER. This is my concern, that we meet this balance, because we have many industries that you're referring to, that you represent, that need these products from China, but we want them at the fair price, not at too high a price, not at a subsidized lower price, but what is the price. I mean, that's what this hearing is about.

Again, Mr. Phelps, China's accession protocol says, quote:

> "If there are special difficulties in that application, the importing WTO member may then use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks.
>
> In applying such methodologies, where practicable, the importing WTO member should adjust such prevailing terms and conditions before considering the use of terms and conditions prevailing outside China."

Close quote.

However, H.R. 1229 changes this test to add, quote:

> "When the administering authority has determined that China is a nonmarket economy country, the administering authority shall presume that special difficulties exist in calculating the amount of a benefit involving China and that it is not practicable to take into account and adjust terms and conditions prevailing in China, and the administering authority shall use terms and conditions prevailing outside of China."

Close quote.

Mr. Phelps, how can this irrefutable presumption be anything but a per se violation of the WTO accession protocol?

Mr. PHELPS. It's hard for me to see how it wouldn't be an illegal, or against the protocol with the WTO accession in China. It's hard for me to see that. I would agree with you.

Mr. HERGER. Again, we're trying to strike this balance. We really want what is right. We want what is fair.

We have many industries that depend on a competitive product from China. We just don't want it to be the other—we don't want it to be too competitive, where they're being subsidized, (a), and (b), we don't want to be put into a position where we go and we're found through a settlement dispute that we're penalized even more.

Can you comment?

Mr. PHELPS. I would agree with that.

The fastest-growing export market for the United States right now is China.

Obviously, it is in our interest—I think it went up 34 percent, exports to China went up 34 percent. It is obviously in our interest to open Chinese markets even further.

If we lose a WTO case, the very first thing they do, countries who win, if they retaliate, is they look at those export industries, and we have a lot of—we're the largest exporting country in the world, and they hit them with duties.

So, I would agree, we really don't want to create more trouble with the WTO for U.S. exporters.

Mr. HERGER. Exactly. Thank you, Mr. Phelps. Thank you, Mr. Chairman.

Chairman LEVIN. Mr. English.

Mr. ENGLISH. Thank you so much, Mr. Chairman. I have a couple of quick questions.

First, Mr. Porter, I'd like to briefly explore a portion of your testimony with you to see if I can clarify your remarks on the so-called pretty much theoretical practice of double counting.

In your testimony, you assert that H.R. 1229 is flawed because it contains no specific provision to, as you say, avoid double counting. You further cite a 2005 GAO study that claims Commerce has no authority under existing law to avoid double counting.

You heard, I presume, Assistant Secretary Spooner testifying earlier that Commerce indeed does, in their view, have the authority to create a methodology for applying countervailing duty laws to nonmarket economies which would take into account the so-called practice of double counting.

In the study that you cite, I believe it also contains a letter from Commerce to the GAO on the report.

Commerce clearly identifies that the best way to address any potential methodology or implementation issues is not through legislation, but rather, quote, "in the context of future cases," unquote, because determining the best methodology would, quote, "hinge in part on the particular facts of any proceeding."

Now, I understand the argument that you've made here is that the Department of Commerce has to evaluate the case for third party—I'm sorry—third country data on a case by case basis. Yet you think Commerce shouldn't be able to make the call on double counting on a case by case basis.

With that, why is it necessary for Congress to tie the hands of Commerce in its implementation of what is, after all, highly complex and difficult administration of this proposal?

Mr. PORTER. Thank you, Congressman.

I apologize if my statement was confusing.

I do not think that Congress should tie the Commerce Department's hands on double counting.

I think there is a, if you will, legitimate disagreement on the interpretation of existing U.S. law on whether, in an individual case, the Commerce Department can make adjustments to account for double counting when the subsidy at issue is a domestic subsidy and not an export subsidy.

There is a specific provision in U.S. law that says you shall not— you shall take into account export subsidies because export subsidies have a direct effect on export price and, at least in theory, it is taken into account with respect to dumping.

Since that provision just says export subsidies, if you will, there is a disagreement on whether Commerce in fact has the authority to take into account, make adjustments for any domestic subsidies that are double counted with respect to dumping.

Congressman——

Mr. ENGLISH. I understand your argument.

Mr. PORTER. I'm sorry, Congressman. What I would suggest is the language used in Section 3 of the prior bill simply says, "Commerce, ensure there's no double counting."

Mr. ENGLISH. I'm sorry, which prior bill?

Mr. PORTER. The one that passed the House, I think it was 3283——

Mr. ENGLISH. Oh, the one I wrote. Okay. I remember that one.

Mr. PORTER. Okay. So, I think that provision simply says, "Commerce ensure there's no double counting. You have the authority to ensure it. We'll leave it to you to decide how to do that."

Mr. ENGLISH. I just question whether that's necessary.

Mr. Hecht, if you would comment on that, and also, you make the comment in your testimony, "Requiring a double counting adjustment, e.g., by always assuming the surrogate values fully account for NME subsidies, could easily place an NME producer in a better position than a similarly situated market economy producer and result in lower assessed unfair trade duties." You attach a chart.

That, of course, would make Mr. Phelps happy, but do you want to comment on that?

Dr. HECHT. Sure, I'd be happy to.

I think that is the case. In a situation where Chinese costs happen to be higher than the surrogate values are, you're absolutely going to be in a situation where China would benefit from the use of a nonmarket economy dumping methodology.

That really is the core insight into why this concern with regard to double counting is in my view misplaced.

The GAO raised what I think is a reasonable question to ask, which is when you're using a surrogate value for a given input, if the Chinese value is subsidized, won't that surrogate value be higher?

That's possible, but what they're not taking into account is you're using a whole lot of other inputs and China may have price distortions where their prices are much higher than the surrogate value.

Mr. ENGLISH. Sure.

Dr. HECHT. The GAO actually issued a study, a year after the one that's been referred to here today, where they looked at the nonmarket economy methodology and they specifically recognized in there that that could be the case, that we really don't know how it's going to cut. It all depends on the facts of a given case.

Here it's easy enough to say that, give them authority to look at it, but the truth is, there is no reasonable basis to determine this, because Commerce does not collect nonmarket economy cost data when it does its analysis, and the whole reason you're using surrogate data is you don't have reliable cost data.

So, the difficulty is, if you require this to be taken into account, there's no way to do that, because you don't have access to the information you need to do it, so it could act to make the law essentially ineffective. That's what the concern is.

Mr. ENGLISH. Thank you, Mr. Chairman, for letting me inquire.

Chairman LEVIN. Not at all, and I think your question highlighted the need to consider what's being said here, and to avoid an argument being raised, it essentially, if followed, would defeat the purpose of the bill.

I don't quite understand the argument that there's a requirement here.

Mr. HERGER. read from this section, from Section 2. What it does is create a presumption.

I don't know how, within anybody's—well, let me put it this way.

I don't see how you turn a presumption into a requirement, or even into a presumption that cannot be rebutted. I don't read the language that way.

So, I think, Mr. Herger, we need to take another look at it, because what I fear is that balance can become an argument for inaction.

Mr. Phelps, I mean, I hear you, and we hear these arguments often.

If you simply look at the impact on the consumer, essentially it makes irrelevant where goods are produced or under what circumstances.

You referred to artificially posted higher prices. The problem is that the imbalance leads to artificially posted higher prices by those who have an unfair advantage over our producers.

I simply want to say to you, and to those you represent, that there is a need, and this is I think what's motivating us very much, to look at the impact of imbalances.

You talk about China as a market for our exports, but—and we went through this with the ambassador who was here, the USTR ambassador. You have to look at what comes in here as well as what goes out.

We have this major imbalance in trade with China, and so does the rest of the world, and it has all kinds of imbalances and all kinds of ramifications, including the ability of entities to use the profits from their sheltered markets to shelter them further.

Dr. HALEY. Can I make a comment?

Chairman LEVIN. Yes.

Dr. HALEY. What I was trying to say was that the subsidies were motivated more by political considerations than by economic ones. So, we do benefit, consumers do benefit, in the short term.

However, the focus of these subsidies will change over the next five to ten years, as they become that of technology acquisition, and they will pose a more strategic threat to the United States, especially in industries in which we are cutting edge.

So, the effects on consumers is just a very minor concern. We have to look at subsidies in a longer term perspective.

Chairman LEVIN. I think well said.

Well, maybe we could carry on this discussion, I won't call it a dialogue——

[Laughter.]

Chairman LEVIN [continuing]. But why don't we do this? If you have any further comments, send them to us. Okay?

We're going to be discussing, and I hope acting on this legislation, in the near future, because all the testimony, virtually all of it, I think Mr. Herger would agree, is that there is a major problem relating to the subsidization by China.

Yes, sir.

Mr. COMRIE. Mr. Chairman, may I make one further comment——

Chairman LEVIN. Please.

Mr. COMRIE [continuing]. Related to this topic?

I think any consideration of this bill would be a mistake if it doesn't consider some aspects of the history of the steel industry.

The steel industry, as I think you well know, from 1950 to 1980, ended up with an industry that was something like 40 percent government owned and ended up in a worldwide glut of steel with major ramifications to customers, major ramifications in this country to the steel industry.

By the mid-1980s, many of those countries that had government-owned steel industries realized this was a terrible mistake, and they went about trying to correct it, and we've gone a long ways in correcting that.

Many of those countries are market economies, but those countries have sort of seen the light and most of them have been privatized.

So, here we are looking at China, who looks like they're going through exactly the same cycle again, only this time many times magnified, much worse, with much worse consequences coming down the road, and we can all see what's almost certain to happen.

So, for anyone to sort of sit here and look at this bill and say that in some way or another the countervailing duty law shouldn't be used to protect the U.S. economy against this cycle that we've already seen happen once just doesn't make any sense.

Chairman LEVIN. All right. We could discuss that. I happen to very much agree with it.

Why don't we do this? We'll recess, not adjourn, so you can further comment.

We really thank you. This, I think, is a vital prelude to what I think will be responsible action in this Congress.

So, thank you very much, and the hearing is now adjourned.

[Whereupon, at 3:45 p.m., the hearing was adjourned.]
[Submissions for the Record follow:]

Statement of Columbia Forest Products

Columbia Forest Products appreciates this opportunity afforded by the U.S. House of Representatives Committee on Ways and Means, Subcommittee on Trade, to voice its views on the application of U.S. countervailing duty laws to imports from countries considered to be "nonmarket economies." Open, constructive dialogue on this issue is essential to ensure that U.S. House of Representative Members are appropriately informed of the important issues addressed by the recently introduced H.R. 1229—the Nonmarket Economy Trade Remedy Act of 2007.

We are confident that this discourse will clearly demonstrate the irrefutable logic underlying the introduced legislation—illegal subsidies injuring U.S. companies must be remedied, regardless of whether the offending country is considered to be a market- or nonmarket-economy.

U.S. companies like ours want an opportunity to participate in a fair global trading community, free of distorting subsidies, in which we can demonstrate the quality of our products and the superior service that we provide our customers. As a business, we recognize that competition is beneficial to ensuring a company's optimal performance. However, competing against companies that receive illegal subsidies is much like being a runner that perfects her performance only to show up on race day to see that her competitor has been allowed a 50-meter head start. Such an unfair advantage would not be allowed in the context of international sports at the Olympic Games, and it should not be allowed in the context of international trade.

The U.S. Department of Commerce has for too long relied on 1984 case precedent, upheld by the U.S. Court of Appeals for the Federal Circuit, to assert that applying countervailing duty laws against nonmarket economies is unfair.

U.S. antidumping laws address illegal dumping from all countries—regardless of "market-economy" or "nonmarket-economy" status. U.S. countervailing duty laws should do the same with illegal subsidies.

We strongly endorse the efforts of Representatives Artur Davis and Phil English to promote a level international trade playing field in which competitive companies can compete and succeed. We beseech the U.S. House of Representatives to quickly pass H.R. 1229.

Respectfully submitted,

Columbia Forest Products

Statement of Erik O. Autor

National Retail Federation
February 7, 2007

The Honorable Sander Levin, Chairman
Ways and Means Trade Subcommittee
U.S. House of Representatives
1102 Longworth HOB
Washington, DC 20515

Dear Chairman Levin:

On behalf of the U.S. retail industry, the National Retail Federation is pleased to provide the following comments to the Ways and Means Trade Subcommittee regarding the hearing on H.R. 1229, the Non-Market Economy Trade Remedy Act of 2007.

By way of background, the **National Retail Federation** is the world's largest retail trade association, with membership that comprises all retail formats and channels of distribution including department, specialty, discount, catalog, Internet, independent stores, chain restaurants, drug stores and grocery stores as well as the industry's key trading partners of retail goods and services. NRF represents an industry with more than 1.6 million U.S. retail establishments, more than 24 million employees—about one in five American workers—and 2006 sales of $4.7 trillion. As the industry umbrella group, NRF also represents more than 100 state, national and international retail associations.

What Is At Stake for the Retail Industry?

Like other businesses, American retailers face the daily challenge of creating value for their customers and shareholders. Retailers must also grow their sales and their businesses in an industry marked by cutthroat competition that creates significant downward pressure on prices, and an average profit margin of 2 percent. To meet these challenges, retailers must offer customers a fresh selection of products—goods they want to buy at prices they are willing and able to pay.

To provide their customers the best selection and value, every American retailer, from the biggest to the smallest, sources products from around the world. Thus, international trade issues fundamentally impact the ability of U.S. retailers to run their businesses successfully. The commercial activity generated by these imports support good-paying, blue and white collar jobs, many of them union jobs. These millions of American workers are employed not only in the retail industry, which accounts for one-fifth of the U.S. workforce, but also in many industries that support retail operations and supply chains—*e.g.,* manufacturing, farming, ports, rail, trucking, warehousing, air delivery, and logistics.

Commerce has historically provided the basis for U.S. economic prosperity. Moreover, the United States today is a consumer-driven economy, with consumer spending accounting for a huge portion of U.S. gross domestic product and economic growth. Nonetheless, we now see a rising sentiment that blames international trade and globalization for a host of economic and competitiveness challenges facing Americans, some having little or nothing to do with trade.

Much of this national economic anxiety is focused on issues in the U.S.-China trade relationship as China becomes a significant player in the global economy. However, few U.S. industries have more at stake in the debate on the U.S.-China trade relationship than retailers. Consumer goods comprise 80 percent of all U.S. imports from China, and China is a key supplier, and sometimes the dominant supplier, in every consumer goods category. Moreover, retailers have been adversely impacted by a recent notable increase in trade remedies investigations (antidumping and safeguards) against imported consumer products—e.g., wooden bedroom furniture, grills, etc—particularly from China.

U.S. Retail Industry Views on H.R. 1229

The Non-Market Trade Remedy Act of 2007 has two major provisions that would make changes to the U.S. trade remedies regime. First, it would statutorily mandate that U.S. countervailing duty (CVD) law applies to China and other non-market economy (NME) countries. Second, it would require Congressional approval of any Administration decision to graduate a NME country to market economy status.

1. *Application of CVD law to NME countries*

To be countervailable, Articles 1.2 and 2.1 of the World Trade Organization (WTO) rules under the Agreement on Subsidies and Countervailing Measures require that a subsidy be "specific to an enterprise or industry or group of enterprises or industries." U.S. countervailing law contains the same specificity requirement.

Since 1984, the U.S. Department of Commerce (DOC) has declined to pursue countervailing duty cases against NME countries under the theory that it is not always possible to identify specific subsidies and calculate their benefits in countries where prices are not set by the market and everything is, in effect, subsidized. Petitioner groups have argued that this policy leaves them no mechanism to offset government subsidies to Chinese industries.

However, NME countries are subject to much more stringent procedures in antidumping cases, which effectively offset any benefit conferred by government subsidies through the use of surrogate country prices to calculate costs of production.

Example: It costs a Chinese company $20 to make a widget, which it sells in the United States at $10, thereby creating a dumping margin of 100 percent. The Chinese Government provides the manufacturer a subsidy of $10 per widget, which lowers its cost of production to $10, the same as its U.S. price. In an antidumping case, DOC will ignore the Chinese company's costs in calculating what the normal value of the widget is in China, and instead use the costs in a surrogate country like India, which are set by the market. If the cost of production in India is $30, the result is not only a higher dumping margin of 200 percent, but, the benefit of the $10 subsidy is completely offset by ignoring the Chinese company's costs.

Given this result, subjecting China and other NME countries to the CVD law raises two problems. First, it appears unfairly biased by essentially treating China as a non-market economy for antidumping cases but as a market economy for CVD cases. This bias raises the question whether this effect would violate the WTO most favored nation principle of non-discrimination. If the United States were to be challenged on this point at the WTO and lose, it would expose U.S. exports to WTO-sanctioned trade retaliation unless the United States eliminated the discriminatory treatment.

The second problem is the issue of double-counting in offsetting the injury from the subsidized imports if there are both antidumping and countervailing duty orders on the same product. It is clear that WTO rules limit a petitioner to one remedy against injury from imports of the same product. Unless the intention is to provide petitioning industries two bites at the apple in attacking imports from China, then the legislation needs to ensure that there is no double-counting of benefits from subsidies between antidumping and CVD cases on the same product. Otherwise, the legislation would run afoul of WTO rules.

In recognition of this problem, a bill passed last year by the House of Representatives contained a provision to prevent double counting, which is not contained in H.R. 1229. While a step in the right direction, this provision only addressed the problem of double counting when simultaneous antidumping and CVD investigations are launched, but not when a CVD investigation is launched against a product already subject to an antidumping order. Although any double-counting could be rectified in this situation by requesting an administrative review, such reviews take time. If the committee determines to approve H.R. 1229, then it is necessary to include a provision to prevent double counting in a comprehensive manner.

2. *Congressional approval required for any change to NME status in antidumping cases*

The concern that appears to underlie the proposal to require Congressional approval of any change to NME status in antidumping cases is that the Administration has allegedly based prior decisions to graduate former NME countries, like Russia, primarily on political rather than economic reasons. This may be a valid concern. It is hard to discern a rationale differentiating Russia that is in the process of renationalizing key sectors of its economy, and China that is continuing the process of privatizing its state owned sectors. The arbitrariness of this question is underscored by the fact that the European Union and Canada already deem China to be a market economy country. Our main concern and question about this provision is that under the guise of trying to eliminate political influence in NME determinations, this change would end up making the process even more political and arbitrary by throwing the decision to Congress.

NRF appreciates the opportunity to comment on H.R. 1229, and looks forward to working with the Ways and Means Committee as it considers this legislation. Should you have any questions please contact me at (202) 626–8104 or by e-mail at autore@nrf.com.

Respectfully submitted,

Erik O. Autor
Vice President, Int'l Trade Counsel

Statement of Nucor Corporation

Nucor Corporation
March 14, 2007

The Honorable Charles B. Rangel
Chairman, Committee on Ways and Means
United States House of Representatives
Washington, DC 20515

The Honorable Jim McCrery
Ranking Member, Committee on Ways and Means
United States House of Representatives
Washington, DC 20515

Dear Chairman Rangel and Ranking Member McCrery:

On behalf of Nucor and its 11,900 employees, I write to express my whole-hearted support for H.R. 1229, the "Nonmarket Economy Trade Remedy Act of 2007." Nucor continues to be deeply concerned about the negative effects of illegal trade practices that are in direct violation of internationally agreed upon rules. We are particularly concerned about the threat posed to U.S. manufacturing from increasing volumes of illegally subsidized Chinese imports. There is simply no reason to exempt China or any other country from the trade laws. This legislation is long overdue and Nucor urges its prompt approval by the Committee and Congress.

China continues to be the main culprit in providing massive illegal subsidies to its steel and other manufacturing industries. Over the past six years, Chinese steel production has risen by 234 percent, and now accounts for nearly 35 percent of global steel production. This unprecedented increase in steel production was possible only because of the enormous subsidies provided by the Chinese government. We are already seeing the impact of this government-sponsored overproduction, with Chinese imports pouring into our market in unprecedented numbers. These imports compete directly with our steel and, while Nucor is as competitive and efficient as any producer in the world, over the long run private industry simply can not compete against the Chinese government.

U.S. trade laws provide a remedy for such illegal and deceptive practices. But the law is not being fully applied—China and other nonmarket economies have been given a free pass because the Commerce Department has chosen not to apply the countervailing duty ("CVD") law to their imports. It is time to end this special treatment and apply the full force of our trade laws to China. H.R. 1229 would do just that. We believe that vigorous application of the CVD law to China is essential to confront the growing threat of unfairly traded Chinese products and to provide U.S. industry an effective remedy against China's illegal and distortive trade practices.

Application of the CVD law to China and other nonmarket economies is entirely consistent with U.S. law and, we believe, required by our international obligations. I'm an engineer, not a lawyer, but it seems to me that we cannot exempt China from the CVD law while applying it to other WTO members. In fact, it is my understanding that China explicitly obligated itself to be subject to CVD investigations when it joined the WTO years ago. Like all of our trading partners, China should be held to the letter of the agreements it signed.

I understand that the Chinese government has raised concerns regarding the application of the CVD law to its imports, including supposed difficulties with identifying and quantifying subsidies. These concerns are nothing more than a smoke screen designed to evade compliance with its WTO obligations. There is no doubt that Chinese government subsidies are quantifiable and measurable. A recent report sponsored by the American Iron and Steel Institute and the Steel Manufacturers Association documented in detail numerous subsidies to China's steel industry, including specific examples of WTO-prohibited subsidies.[1] More importantly, China itself identified more than 75 types of subsidies in its April 2006 subsidies notification to the WTO. The notification confirmed that China continues to provide a broad range of subsidies contingent on export performance, even though such subsidies are prohibited by the WTO. If China can identify them, so can we!

By continuing to exempt China and other nonmarket economies from application of the CVD law, the United States sends the message that countries can violate international and U.S. trade laws with impunity. This bill would change that by ensuring that there are no more free passes for China and other nonmarket economies that systematically violate our trade laws by subsidizing their manufacturers. I would also like to express Nucor's support for the so-called "graduation" provision in this bill, which would require Congressional approval of a determination by the Department of Commerce to revoke a country's nonmarket economy status under U.S. antidumping law. This provision would ensure that Commerce follows the criteria required by law for promoting countries to market economy status and that Congress has a say in such an important decision.

In summary, Nucor urges prompt passage of H.R. 1229. Application of the full range of trade remedies available under the law is critical to countering the serious threat to U.S. industry posed by unfairly subsidized Chinese imports. Applying the CVD law to China and other nonmarket economies will help end the significant distortions in global trade flows caused by enormous government subsidies. Bringing a rapid end to these illegal and damaging practices is essential to the future health and prosperity of the U.S. steel industry and U.S. manufacturing in general.

Sincerely,

Daniel R. DiMicco
Chairman, President, and Chief Executive Officer

[1] *See The China Syndrome: How Subsidies and Government Intervention Created the World's Largest Steel Industry,* available at http://www.wileyrein.com/docs/docs/80.pdf.

Statement of Retail Industry Leaders Association

The Retail Industry Leaders Association (RILA) welcomes the opportunity to submit comments on the application of the countervailing duty law to imports from non-market economy countries, with a focus on H.R. 1229, the "Non-market Economy Trade Remedy Act of 2007." While RILA recognizes that policymakers should ensure that U.S. producers have the tools necessary to address unfair trade, it is equally important that such tools are drafted and administered objectively and in line with U.S. international obligations.

RILA opposes H.R. 1229 in its current form because it goes well beyond simply applying the countervailing duty law to non-market economies. The bill, as introduced, prescribes an unfair methodology for calculating subsidies and inserts a Congressional role into the administration of trade remedy laws—procedures which should more appropriately remain the subject of objective, quasi-judicial proceedings at the U.S. Department of Commerce (DOC) and the U.S. International Trade Commission.

By way of background, RILA promotes consumer choice and economic freedom through public policy and industry operational excellence. Our members include the largest and fastest growing companies in the retail industry—retailers, product manufacturers, and service suppliers—which together account for more than $1.5 trillion in annual sales. RILA members provide millions of jobs and operate more than 100,000 stores, manufacturing facilities and distribution centers, have facilities in all 50 states, and provide millions of jobs domestically and worldwide. Our members pay billions of dollars in federal, state and local taxes and collect and remit billions more in sales taxes. Our members are also leading corporate citizens with some of the nation's most far-reaching community outreach and corporate social responsibility initiatives.

The retail sector, along with the suppliers and customers that it serves, is an essential part of the U.S. economy. Retailers meet the needs of U.S. consumers, and in doing so are essential drivers of the U.S. economy. We also serve the global market for consumer goods and bring U.S. products to the foreign markets where they operate. Retailers provide quality jobs at all employment levels with good benefits. The industry also creates opportunities for entry-level employment, part-time work, jobs for non-skilled workers, and management training for front-line workers.

Congressional Vote on Market Economy Status

The most concering provision in H.R. 1229 is the requirement for Congressional approval for any change in non-market economy status in antidumping and countervailing duty cases. Proponents of this measure claim that Congressional action is required to prevent the Administration from making decisions based on political interests rather than economic facts. However, such a provision would intrinsically raise the level of political interference in these decisions. The DOC is much better prepared to objectively analyze the statutory criteria that determine whether a country should be considered a market economy, such as currency convertability, whether wage rates are established by free bargaining, the extent of joint ventures and foreign investments, and the extent of government ownership or control of production and of the allocation of resources. The trade analysts at the DOC have the information, analysis, and expertise to evaluate these technical economic issues. It is false to suggest that Members of Congress would be better positioned to make such an assessment.

Application of Countervailing Duty Law to Non-Market Economy Countries

It is appropriate to have in place tools that address unfairly subsidized trade and can provide relief to U.S. producers that are injured. To be sure, U.S. policy should discourage foreign governments from intervening in private enterprise through subsidies and other actions. Nevertheless, RILA believes that H.R. 1229, as introduced, does not provide an appropriate legal platform for the Department of Commerce to conduct a technical analysis of the facts of specific subsidy cases against imports from non-market economies. Any effort to apply the countervailing duty law to non-market economies should not be undertaken in a vacuum.

Continuing to employ a non-market economy methodology in antidumping proceedings while also applying the countervailing duty law to the same product from the same country requires analysts to carefully identify whether and how there may be double counting for the same government interventions in the marketplace. The Government Accountability Office (GAO) recognized this potential problem in its report entitled "U.S.-China Trade: Commerce Faces Practical and Legal Challenges in Applying Countervailing Duties" (GAO–05–474). Specifically, unlike antidumping cases that involve market economy countries, the antidumping methodology for non-market economy countries also accounts for government intervention in the marketplace, so blanket authority for a subsidy analysis of the same imports would inevitably count certain behavior twice.

RILA suggests that better legal language to apply the countervailing duty law to non-market economies can be found in Section 3 of H.R. 3283 in the 109th Congress, which passed the House of Representatives in July 2005 by a vote of 255–168. As with H.R. 1229, Section 3 of H.R. 3283 would also give United States producers access to relief that directly targets government subsidies. At the same time, it also addresses the GAO's concern regarding potential double counting, and ensures that any relief from subsidized imports is granted in an objective and fair manner, and in line with U.S. multilateral obligations. Such prudent measures are beneficial to the U.S. trade remedy regime because they would decrease the likelihood that any relief granted would be subject to time-consuming and burdensome legal challenges in U.S. courts and in the World Trade Organization (WTO).

Additionally, Section 3 of H.R. 3283 implements another GAO recommendation to explicitly give the Commerce Department the authority to use third-country benchmarks to measure government subsidies in China. The bill also carefully tracks the commitment U.S. negotiators secured from China when it acceded to the WTO. While H.R. 1229 also provides for third-country benchmarks, it inappropriately requires the DOC to presume that any subsidies conferred in a non-market economy should be measured by benchmarks in surrogate countries. Such an approach is significantly more likely to be challenged in the WTO because it does not track international agreements. Issues such as appropriate benchmarks should be left to experts at the DOC, and those analysts should endeavor to make an objective analysis to determine the most appropriate benchmark rates to most accurately measure any subsidy conferred.

Conclusion

RILA recognizes that U.S. producers that are harmed by subsidized imports should have access to remedies that directly address such unfair trade. RILA does not oppose an effort to simply apply the countervailing duty law to non-market economy countries. At the same time, it is unclear whether legislation is actually required to do so. In fact, the DOC is already currently investigating allegations of Chinese subsidies to its paper industry. Further, RILA believes that if legislation does move forward to apply the countervailing duty law to non-market economies, the Committee should endeavor to make the legislation objective and consistent with international obligations. Section 3 of H.R. 3283 from the 109th Congress is a much better alternative to achieve this goal than H.R. 1229. If you have any questions on this statement or require any assistance, please contact Lori Denham, Executive Vice President, Public Policy and Industry Operations at, or Andrew Szente, Director, Government Affairs.

Statement of Society of the Plastics Industry

Society of the Plastics Industry
March 29, 2007

Chairman Sander Levin
Trade Subcommittee
Committee of Ways and Means
U.S. House of Representatives
1102 Longworth House Office Building
Washington, DC 20515

Dear Chairman Levin:

Thank you for this opportunity to submit comments on H.R. 1229, the "Non-Market Economy Trade Remedy Act of 2007." The Society of the Plastics Industry (SPI), as the primary association representing the U.S. plastics industry, urges Congress to adopt legislation that directs the Commerce Department to apply countervailing duties to unfairly subsidized and injurious imports from non-market economy countries such as China. SPI believes that this legislation is necessary for the U.S. plastics industry because it allows the U.S. government to counteract the negative impact of subsidies provided by important non-market economies to their manufacturers.

The production of plastics materials and plastics products is the third-largest manufacturing industry in the United States. SPI is the only national plastics trade association representing companies that operate in all segments of the plastics supply chain—processors, manufacturers of machinery, molds, and raw materials (resins/polymers). SPI members range from large multinational corporations to small and medium-sized companies, many of which are family-owned businesses, all playing a vital role in the delivery of myriad plastics products that enhance every aspect of our lives.

China is a significant market for the U.S. plastics industry. In 2003, China became the third largest export market for plastics industry goods, with exports valued at $1.32 billion.[1] This export growth continued in the past three years, leading to U.S. plastics exports worth $2.8 billion in 2006. Despite this robust growth in exports, the U.S. plastics industry is experiencing a very large and growing bilateral trade deficit with China, which amounted to $5.6 billion in 2006. The bilateral trade deficit is even more pronounced in processed plastic products, reaching $7.2 billion in 2006.

The U.S. plastics industry is experiencing significant disadvantages in the global marketplace caused by unfairly subsidized exports from non-market economies, such as China. SPI members believe that manufacturers injured by unfair subsidization should have an effective mechanism to remedy their harm. Although passage of H.R. 1229 by itself will not alleviate all of the plastics industry's pressures, addressing the subsidies and other unfair practices of trading partners can certainly improve the competitive position of U.S. plastics manufacturers and, in turn, save and create jobs.

Plastics manufacturing is a technologically-advanced and capital-intensive industry able and willing to compete in the global marketplace. However, countries like China are providing an unfair advantage to their exporters by maintaining an artificially low level of their currencies. Along with high natural gas and energy prices, this has been an external pressure that has unnecessarily burdened the industry's competitiveness. As the artificially undervalued currency of China and other Asian countries affects sales by plastics companies both in their domestic market and abroad, SPI urges Congress to specifically designate exchange rate misalignment as an export subsidy actionable under the U.S. countervailing duty statute. SPI strongly supports the legislative approach undertaken by Representatives Tim Ryan and Duncan Hunter in the "Fair Currency Act of 2007" (H.R. 782).

If left unchecked, the challenges posed by unfair industry subsidization and currency misalignment in non-market economies threaten the survival of an American industry that generates approximately $341 billion in annual revenues and directly employs 1.1 million people. By allowing the application of the U.S. countervailing statute to China and other non-market economies, H.R. 1229 will unambiguously demonstrate Congress's commitment to combating unfair trade practices and enhancing the competitiveness of the U.S. manufacturing sector. The passage of H.R. 782 would further build on this approach by providing a tool to U.S. manufacturers to address a critical problem that they face in the global marketplace.

We appreciate the opportunity to comment on this issue and hope that the Committee on Ways and Means finds this information helpful as it considers whether the CVD law should be applied to non-market economies. If you would like additional information from SPI or have questions, please do not hesitate to contact SPI.

Respectfully submitted,

Bill Carteaux
William R. Carteaux
President and CEO

[1] Unless otherwise noted, "plastics industry goods" refers to products falling under four categories: resins/raw materials (HTS 3901–3915); plastics products—intermediate and final goods (HTS 3916–3926); plastics machinery and parts (HTS 8477, 8479); and plastics molds (HTS 8480).

Statement of Southern Shrimp Alliance, Inc.

Southern Shrimp Alliance, Inc.
Tarpon Springs, Florida 34688
March 23, 2007

The Honorable Sander M. Levin, Subcommittee Chairman
Subcommittee on Trade,
Committee on Ways and Means,
U.S. House of Representatives
1102 Longworth House Office Building
Washington, DC 20515

Dear Chairman Levin:

In response to the Subcommittee's March 7, 2007 announcement of hearing and opportunity for comments, the Southern Shrimp Alliance hereby submits written comments in support of The Nonmarket Economy Trade Remedy Act of 2007. SSA supports application of the countervailing duty law to imports from nonmarket economy countries. While the attached comments submitted to the U.S. Department of Commerce make clear that change in legislation is not required, amending the law would resolve any lingering questions about the legality of extending the countervailing duty law to nonmarket economies.

The United States has recognized the existence of a number of subsidies in China by its requests for consultations before the World Trade Organization. The large and growing trade deficit, particularly with China, and the existence of trade-distorting subsidies in nonmarket economies demonstrate the need to remove any possible legal impediment to addressing subsidies in nonmarket economies through the countervailing duty law.

SSA appreciates the opportunity to comment on pending legislation. Please contact the undersigned if you have any questions regarding this submission.

Respectfully submitted,

John Williams
Executive Director

Statement of Zygmunt Jablonski

My name is Zygmunt Jablonski, Executive Vice President and General Counsel of Unisource Worldwide, Inc. Prior to my employment with Georgia-Pacific and with Unisource, I was an international trade attorney in private practice in Washington, D.C. It is a pleasure to discuss U.S. trade remedy laws and H.R. 1229.

Unisource is one of the largest independent paper, packaging and facility supplies distribution companies in the United States. In 2006, our sales were nearly $6 billion of which paper products represent roughly 60 percent of total sales. We have 75 locations across the country, a fleet of approximately 1300 vehicles, and we have about 5000 employees in the United States.

We buy and sell products from both U.S. producers and foreign suppliers. When it comes to paper products—such as coated free sheet paper—we purchase more of our products domestically than we import.

I raise this issue because it is important to consider the business climate in which we operate as the Committee considers this legislation. At the outset, I want to make clear that we fully recognize the need to ensure that imports are fairly traded. We would support a law that allows investigations of whether imports from nonmarket economies have been unfairly subsidized. Our objective is to ensure that legislation does not impose unreasonable standards on imported products. So, we support a level playing field for our domestic suppliers but we do not support a playing field which tilts the other way and is unfair to our foreign suppliers. As currently drafted, we believe that H.R. 1229 does not strike an appropriate balance.

I would like to raise two technical issues and one fundamental issue with the current legislation. First, the bill requires the Commerce Department to calculate the CVD rate for non-market economies, like China, by using benchmarks outside of China. In our view, whether subsidies exist, and how to value them, should primarily be based on whether there is preferential treatment vis-à-vis other domestic enterprises, as in the case with market economies and other WTO members. Anti-subsidy rules, including WTO rules, do not preclude governments from providing benefits as long as those benefits are not specific to a particular industry. H.R. 1229 would penalize the Chinese government by disregarding domestic benchmarks that would be used for all other WTO members. In addition, prohibiting Commerce from using benchmarks from China ignores the market reforms that have taken place in China. Today, there are many companies in China that are completely private, foreign owned and operate according to market economy principles.

Second, H.R. 1229 does not prevent double counting of duties in situations in which the same exporters face both an antidumping and a CVD case. The bill would impose two sets of duties to compensate for the same unfair trade practice. As you know, GAO confirmed that such a framework would result in an unfair double counting. U.S. courts have suggested that such double counting is generally considered improper, and such double counting would also expose the United States to a challenge in the WTO that it would likely lose.

To address these issues, I respectfully suggest that the legislation authorize the Commerce Department to offset those elements of the subsidies which are fully accounted for in the use of surrogate values to calculate the dumping margins. The need to offset any double counting is already recognized in existing law by allowing Commerce to offset export subsidies against antidumping margins. Likewise, in the non-market economy context, a similar authority is necessary to allow Commerce to offset non-export subsidies against antidumping margins that already take into account such non-export subsidies. The ability to offset would help provide a level playing field and reflect the principles of fair trade.

In addition to the technical issues I just raised, I would like to close by discussing a fundamental economic contradiction in H.R. 1229. We do not believe that Commerce should apply the CVD law to China as long as China is treated as an NME for purposes of the antidumping law. Among the specific factors that the Commerce Department has examined in treating China as a non-market economy, of direct relevance to application of the countervailing duty law is the convertibility of the local currency, in this case the *renminbi,* which reflects its reliability as a measure of international market value. Domestic prices and costs denominated in what the Commerce Department deems to be an unreliable currency are nevertheless the very values that the Department would rely upon to calculate any subsidy benefit in a CVD investigation.

For example, when Commerce determines the benefit from a tax program that is alleged to confer a countervailable subsidy, the actual tax paid is a function of sales revenues and production costs that may be denominated in both the local currency and foreign currencies. Yet Commerce does not consider the foreign currency to be comparable to international currencies. How is it that Commerce would rely upon figures derived from locally-denominated prices in the countervailing duty context if it has determined that the prices are so distorted in the antidumping context that they cannot be used to determine reliable values? Yet that inconsistency is what the bill would require.

Thank you for this opportunity to present our views on this important matter.