SUBSIDIES ENFORCEMENT
ANNUAL REPORT TO THE CONGRESS

Joint Report of the
Office of the United States Trade Representative
and the U.S. Department of Commerce
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EXECUTIVE SUMMARY

The Office of the U.S. Trade Representative (USTR) and the U.S. Department of Commerce (Commerce) submit a joint report to the Congress each year that describes the Administration's subsidy monitoring and enforcement activities throughout the previous year. This report, mandated by section 281(f)(4) of the Uruguay Round Agreements Act, is the twelfth annual report submitted to the Congress.

The use of unfair trade-distorting practices, including subsidies, continues to pose a competitive challenge for American workers and industries. The United States Government is committed to eliminating or neutralizing such practices when they adversely impact U.S. interests by pursuing its rights under the agreements of the World Trade Organization (WTO) and by ensuring that the United States' trading partners adhere to their obligations under those agreements. This report describes the efforts by USTR and Commerce, in close cooperation with other Executive Branch agencies, to monitor and challenge unfair foreign government subsidy practices worldwide in 2006.

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

Another key and ongoing focus of the subsidies enforcement program is to address the root causes that give rise to unfair trade distortions. In this regard, the United States continued its efforts to strengthen and deepen multilateral disciplines on subsidies through the Doha Development Agenda negotiations. These efforts will help expand and deepen the open, competitive and market-oriented trading environment that provides benefits to American consumers, producers and workers alike.

Doha Development Agenda

In November 2001, the latest round of global trade negotiations – known as the Doha Development Agenda (DDA) – was launched at the WTO's Fourth Ministerial Conference. In the Doha Ministerial Declaration, the United States secured a mandate to clarify and improve the disciplines under the Subsidies Agreement and address the trade-distorting practices that often give rise to the imposition of countervailing and antidumping duties. Importantly, the WTO rules negotiating mandate recognizes that the negotiations must preserve the basic concepts, principles and effectiveness of the

Subsidies Agreement and the Agreement on Implementation of Article VI of the GATT 1994 (Antidumping Agreement) and that Members' trade remedy laws are legitimate tools for addressing unfair trade practices that cause injury.

In March of 2003, the United States submitted its principal proposal on subsidies to the Rules Negotiating Group (Rules Group). That submission outlined the basic objectives for the United States in seeking to strengthen the subsidy rules. The United States called for enhanced subsidy disciplines and identified a broad array of issues with respect to the existing rules, as well as the need to develop new disciplines where none currently exist. The United States' negotiating position on subsidies addresses issues that relate to the negotiating objectives set forth in the Trade Act of 2002 (which encompasses Trade Promotion Authority), including the existing rules on the treatment of indirect taxes. In particular, the U.S. argued for the expansion of the prohibited ("red light") category of subsidies, and tougher rules on indirect subsidies, government investment in private sector companies, and government pricing of natural resources.

Beginning in 2004 and continuing through 2006, the United States made various submissions specifically focusing on the further development of subsidy calculation methodologies so as to clarify the precise nature of Members' obligations under the Subsidies Agreement and to establish a firmer basis for strengthened rules (*e.g.,* quantitative limitations on subsidy benefit amounts). The U.S. submissions covered the related topics of when, and how, to allocate a subsidy benefit over time. In an April 2006 paper, the most recent submission to date on this topic, the United States submitted possible draft text for how these proposals on subsidies allocation could be incorporated into the Subsidies Agreement. The paper was subject to an in-depth technical examination in the Rules Group and was well received by other WTO Members.

In January 2006, the United States also submitted a follow-up proposal regarding prohibited subsidies. Noting that serious market and trade distortions can result from particular types of subsidies other than those currently prohibited by the Subsidies Agreement (*i.e.,* export subsidies and import-substitution subsidies), the United States called upon Members to consider expanding the current prohibition to encompass other subsidies that most typically and directly forestall or impede industry restructuring and rationalization. Among these, the United States suggested consideration of subsidies practices similar to those listed in the now-lapsed "dark amber" provisions of the Subsidies Agreement (*e.g.,* government debt forgiveness) and other forms of egregious government intervention. In addition to proposing the expansion of the prohibited category, the proposal also laid out a bold new approach to address the United States' increasing concerns with foreign state-owned and state-controlled enterprises. The paper asserted that private sector government investment decisions that run counter to the market's assessment should be made transparent, closely scrutinized and, as appropriate, curtailed. Accordingly, *inter alia*, the paper proposed that WTO Members be required to notify the WTO Subsidies Committee of any government equity investment.

The U.S. submission is one of the most far-reaching subsidy-related proposals tabled to date in the Rules negotiations, reinforcing the United States' leadership role in pursuing strong subsidies disciplines in the WTO. The strengthened disciplines proposed would greatly enhance the United States' ability to address, and potentially deter, subsidy-related unfair trade practices confronting U.S. industries. Conditional on the resumption and progress of work in the Rules Group overall, we intend to follow up on the January 2006 prohibited subsidies paper with a proposal containing draft text for how such an expanded prohibition could be incorporated into the Subsidies Agreement. Other important proposals to clarify and improve the Subsidies Agreement were made in 2006 by Australia, Canada, Brazil, the European Union, Chinese Taipei, in addition to a joint proposal by India, Egypt, Kenya and Pakistan.

As to the fisheries subsidies negotiations within the Rules Group, the United States continued to play a major leadership role in advancing the discussion in 2006, working closely with a broad coalition of developed and developing countries.[1] The United States views these negotiations as a groundbreaking opportunity for the WTO to show that trade liberalization can benefit the environment and contribute to sustainable development as well as address traditional trade concerns. In the Rules Group, there continues to be a discussion of possible frameworks for improved disciplines. The United States and other proponents of stronger disciplines have been advocating a framework that would center on a broad-based prohibition, combined with appropriate exceptions (generally referred to as the "top down" approach). Negotiators also examined particular categories of fisheries programs and how they might be treated under new disciplines. In this context, in April 2006, the United States submitted an additional paper with proposed draft text to address three technical issues relating to stronger fisheries subsidy disciplines.

At the Hong Kong Ministerial Conference in December 2005, Ministers directed the Rules Group to intensify and accelerate the negotiating process in all areas of its mandate, on the basis of detailed textual proposals, and to complete the process of analyzing proposals as soon as possible. Ministers also directed the Rules Chairman to prepare consolidated texts of the Antidumping and Subsidies Agreements, taking account of progress in other areas of the negotiations. While the Group intensified its work in early 2006 in accordance with the Hong Kong Declaration, the Rules Chairman did not issue consolidated texts of the Antidumping and Subsidies Agreements in 2006, given the suspension of work in the Doha negotiations in July 2006.

As of January 2007, the outlook and timing of any formal resumption of the Doha Agenda negotiations remain uncertain. Some ongoing work has continued at the technical level. If there is a breakthrough in other key negotiating areas, and thus a full

[1] The informal group of countries supporting stronger disciplines on fisheries subsidies, known as the "Friends of Fish," includes the United States, Argentina, Australia, Chile, Ecuador, Iceland, New Zealand and Peru.

resumption of the Doha Agenda negotiation, the United States will be prepared to continue its active participation in the Rules negotiations.

China

In 2006, China concluded its fifth year of membership in the WTO and the fifth examination of the implementation of its accession commitments under the Transitional Review Mechanism (TRM). The fifth annual review in the Subsidies Committee took place in October and the United States used that opportunity to address a number of subsidy-related issues, including China's long-overdue subsidies notification, submitted to the Subsidies Committee in April 2006. The United States' continued efforts to monitor and analyze China's subsidy practices significantly facilitated the analysis of the information provided and the identification of programs not included in the notification. Although China notified over 70 subsidy programs, it failed to notify any subsidies provided by China's state-owned banks or by provincial and local government authorities. In addition, while China notified several subsidies that appear to be prohibited, it did so without making any commitment to withdraw them.

The United States urged China to withdraw both the prohibited subsidies that it had notified and several additional prohibited subsidies that it had not notified. Through a series of bilateral meetings in Beijing, including high-level meetings, the United States made clear that China needed to withdraw all of its prohibited subsidies. Although these exchanges helped to clarify certain issues, China has been unwilling to commit to the immediate withdrawal of the prohibited subsidies in question. The United States continues to press China on this issue and will take further action to end these prohibited subsidies.

In October 2006, a petition was filed with Commerce requesting the initiation of a countervailing duty (CVD) investigation, based on allegations of injurious subsidized imports of coated free sheet paper from China. The petition notes that Commerce currently does not apply the U.S. CVD law to nonmarket economies such as China's, and requests a change in that policy. In November 2006, Commerce initiated an investigation, and will, in the course of the investigation, consider the question of the applicability of the CVD law to China. Given the complex legal and policy issues involved, Commerce requested public comment on the issue of the application of the CVD law to nonmarket economies, such as China, and as of January 16, received comments from over 50 parties. Commerce will carefully review all of these submissions during the course of this proceeding.

In 2007, the United States will intensify its efforts to identify and analyze Chinese subsidy programs. These efforts will enhance the United States' ability to engage China regarding its subsidies practices and confront those that are inconsistent with its obligations. The United States will also continue to raise its concerns at the WTO and in bilateral meetings with China, as necessary, including through upcoming meetings of

the Structural Issues Working Group (SIWG) established under the U.S.-China Joint Commission on Commerce and Trade (JCCT) in April of 2004. With a renewed emphasis on this working group emerging from the newly initiated Strategic Economic Dialogue with China, Commerce and USTR plan to devote considerable attention and resources to subsidy-related issues in this working group in 2007.

Steel

During 2006, the United States continued to be a key player in international efforts to address the structural issues which plague the global steel industry, particularly with respect to the frequency and magnitude of market-distorting government intervention in this market. Consistent with the President's 2001 Initiative on Steel, the primary goal of these efforts is to seek more lasting solutions to the historical long-term problems in this industry, including oversupply, unfair trade competition and trade remedy responses. The United States was very active this past year in multilateral, regional, and bilateral efforts to bring about market-driven rationalization of the world's excess, inefficient steelmaking capacity and to push for formulating better disciplines on market- and trade-distorting practices. The North American Steel Trade Committee (NASTC) and the OECD Steel Committee continue to be valuable fora for exploring ways to address the structural problems of the industry. In addition, this past year the United States initiated a U.S.-China Steel Dialogue under the JCCT to engage the Chinese government and industry on issues including the problems that subsidies and other types of government intervention in the steel sector can cause in world steel markets.

Conclusion

The U.S. Government's subsidies enforcement program is committed to assisting American workers and companies that are threatened or harmed by distortive subsidy practices, both domestically and in foreign markets. Therefore, USTR and Commerce will continue to identify and challenge those unfair foreign government practices that adversely affect the interests of the United States, whether through advocacy, negotiation or legal action. These activities are primarily designed to help those U.S. parties that face particular problems from subsidized competition without unduly imposing additional costs and obstacles to international commerce and investment. The United States' preference is to resolve these issues through advocacy, negotiation or bilateral or multilateral contacts. However, the United States will not refrain from initiating WTO dispute settlement proceedings if its interests cannot be adequately addressed through advocacy and negotiation.

The United States will continue to strengthen its efforts to ensure that American consumers, workers and companies benefit from a competitive, market-oriented global economy that is free of distortions brought on by unfair trade practices such as subsidies. This commitment will be strengthened by more effectively focusing U.S.

Government resources to identify and challenge a wide range of unfair foreign government practices that adversely affect the interests of the United States. In doing so, we will also help ensure that U.S. consumers enjoy the full range of choice, quality and affordable prices that can only be obtained through engagement in a dynamic and competitive global economy.

INTRODUCTION

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

The Subsidies Agreement nominally divides subsidy practices among three classes: prohibited (red light) subsidies; permitted yet actionable (yellow light) subsidies; and permitted, non-actionable (green light) subsidies.[2] Export subsidies and import substitution subsidies are prohibited. All other subsidies are permitted, but are actionable (through CVD or dispute settlement action) if they are (I) "specific", *i.e.*, limited to a firm, industry or group thereof within the territory of a WTO Member and (ii) found to cause adverse trade effects, such as material injury to a domestic industry or serious prejudice to the trade interests of another WTO Member. With the expiration of the Agreement's provisions on green light subsidies, at present, the only non-actionable subsidies are those which are not specific, as defined above.

U.S. trade policy responses to the problems associated with foreign subsidized competition provide USTR and Commerce with both unique and complementary roles. In general, it is USTR's role to coordinate the development and implementation of overall U.S. trade policy with respect to subsidy matters, represent the United States in the WTO, including its Subsidies Committee, and chair the interagency process on matters of trade policy. The role of Commerce, through the International Trade Administration's Import Administration (IA), is to enforce the CVD law, monitor the subsidy practices of other countries, and provide the technical expertise needed to analyze and understand the impact of foreign subsidies on U.S. commerce. IA will also

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[2] Prior to 2000, Article 8 of the Agreement provided that certain limited kinds of government assistance granted for industrial research and development (R&D), regional development, or environmental compliance purposes would be treated as non-actionable subsidies. In addition, Article 6.1 of the Agreement provided that certain other subsidies (*e.g.,* subsidies to cover a firm's operating losses), referred to as dark amber subsidies, could be presumed to cause serious prejudice. If such subsidies were challenged on the basis of these dark amber provisions in a WTO dispute settlement proceeding, the subsidizing government would have the burden of showing that serious prejudice had *not* resulted from the subsidy. However, as explained in the 1999 Annual Subsidies Report, these provisions expired on January 1, 2000, because a consensus could not be reached among WTO Members on whether to extend these provisions, or on the terms by which these provisions might be extended beyond their five-year period of provisional application.

provide assistance and advice to interested U.S. parties concerning the remedies available under the Subsidies Agreement and the procedures relating to these remedies and, where warranted, recommend action to USTR.

Within IA, subsidy monitoring and enforcement activities are carried out by the Subsidies Enforcement Office (SEO). These activities are supported and complemented by the Trade Remedy Compliance Staff (TRCS), also located in IA. (See, Attachments 1 and 2, which contain full descriptions of the SEO and TRCS.) IA continues to build upon and improve coordination of these different efforts to pro-actively address foreign unfair trade practices. In 2004, IA created the Unfair Trade Practices Task Force, which has further enhanced Commerce's ability to aggressively track foreign unfair trade practices and develop strategies to address them. USTR and Commerce also work closely with, and receive valuable input and advice from, other federal agencies represented in the Trade Policy Staff Committee – such as the Departments of State, Treasury and Agriculture, and Council of Economic Advisors – concerning the full range of issues pertaining to the obligations of the United States' trading partners under the Subsidies Agreement.

The enactment of the Uruguay Round Agreements Act (URAA) in 1994 provided USTR and Commerce additional scope and focus in order to facilitate the exercise of U.S. multilateral rights with respect to subsidies that harm the interests of U.S. firms and workers. Among the joint responsibilities assigned to USTR and Commerce, as set forth in section 281(f)(4) of the URAA, is the submission of an annual report to the Congress describing the United States' monitoring and enforcement activities throughout the previous year. This report constitutes the twelfth annual report to be transmitted to the Congress pursuant to this provision.

MULTILATERAL INITIATIVES

A. WTO NEGOTIATIONS

In November 2001, the latest round of global trade negotiations – known as the Doha Development Agenda (DDA) – was launched at the WTO's Fourth Ministerial Conference. In the Doha Ministerial declaration, the United States secured a mandate to clarify and improve the disciplines under the Subsidies Agreement and to address the trade-distorting practices that often give rise to the imposition of countervailing and antidumping duties. Critically, the WTO rules negotiating mandate recognizes that the negotiations must preserve the basic concepts, principles and effectiveness of the Subsidies and AD Agreements and that Members' trade remedy laws are legitimate tools for addressing unfair trade practices that cause injury. Under this mandate, the United States has continued to pursue an aggressive, affirmative agenda, aimed at strengthening the rules and addressing the underlying causes of unfair trade practices.

The existing WTO disciplines on subsidies prohibit only two types of subsidies. However, other permitted subsidies can also distort markets and international trade patterns. The specific language of the mandate agreed to at the Fourth Ministerial Conference is particularly important because it provides an avenue to address these other practices and to inform the discussions of trade remedies in a constructive manner. Moreover, it provides an avenue to take up the negotiating objectives of the Trade Act of 2002 and other subsidy concerns that affect key sectors of the U.S. economy.

Another important component of the DDA is the discussion of disciplines on fisheries subsidies, which is included as part of the Rules negotiations. The United States has believed for some time that the depleted state of the world's fisheries stock is a major economic and environmental concern, and that subsidies that contribute to overcapacity and overfishing, or that have other trade-distorting effects, are a significant part of the problem. The inclusion of fisheries subsidies in the Rules negotiations represents a significant opportunity for all countries to advance simultaneously the goals of trade liberalization, environmental protection, and economic development.

1. Progress to Date

a. General

The Rules Group has based its work primarily on the written submissions from Members, with the work organized into the following categories: (1) antidumping (often including similar issues relating to countervailing duty remedies); (2) subsidies, including fisheries subsidies; and (3) regional trade agreements. At the Hong Kong Ministerial Conference in December 2005, Ministers directed the Rules Group to intensify and accelerate the negotiating process in all areas of its mandate, on the basis of detailed textual proposals presently before the Group, or yet to be submitted, and to complete the process of analyzing proposals as soon as possible. Ministers also mandated the Rules Chairman to prepare consolidated texts of the AD and Subsidies Agreements early enough to ensure a timely outcome within the context of the then-presumed 2006 end date for the Doha Agenda negotiations and taking account of progress in other areas of the negotiations.

In 2006, under the chairmanship of Ambassador Guillermo Valles Galmes of Uruguay, there were several meetings of the Rules Group, mostly during the first half of the year. Continuing the trend from earlier years, during this time the Rules Group met only infrequently in "formal" sessions, preferring "informal" and "plurilateral" sessions (comprised of smaller groupings of Members who have shown the most interest in a particular negotiating topic) that facilitate more detailed discussion in an effort to winnow the considerable number of proposals and to focus on specific text-based proposals. While the Group intensified its work in early 2006 in accordance with the Hong Kong Declaration, the Rules Chairman did not issue consolidated texts of the

Antidumping and Subsidies Agreements in 2006, given the suspension of work in the Doha negotiations in July 2006.

As of January 2007, the outlook and timing of any formal resumption of the Doha Agenda negotiations remain uncertain. Some ongoing work has continued at the technical level to discuss issues relating to fisheries subsidies. Another informal meeting has been scheduled for February 2007 to further discuss general subsidies and fisheries subsidies issues. If there is a breakthrough in the key negotiating areas other than Rules, permitting a full resumption of the Doha Agenda negotiation, the United States will be prepared to continue its active participation.

b. U.S. Subsidies-Specific Submissions

As part of its active involvement in the Rules negotiations, the United States has submitted several subsidies-specific papers and proposals, starting with a U.S. submission in December 2002 on special and differential treatment for developing countries.[3] In March 2003, the United States submitted its second subsidies-specific paper on the general need for improved disciplines.[4] In this paper, the United States identified a broad array of subsidy issues with respect to the existing rules, and suggested areas for new disciplines where none currently exist. The U.S. position on subsidies is firmly grounded in the negotiating objectives of the Trade Act of 2002. As noted above, the development of enhanced disciplines on trade-distorting practices, including subsidies, is particularly important because these practices are often the root cause of trade friction.[5]

In the years 2004 through 2006, the United States made six additional written submissions, the first five of which specifically focused on the further development of subsidy calculation methodologies. While the Uruguay Round negotiations were successful in defining broad methodological concepts in the Subsidies Agreement regarding the measurement of various types of subsidies, the United States believes that greater detail is needed in certain areas to clarify the precise nature of Members' obligations under the Subsidies Agreement and to establish a firmer basis for strengthened rules (*e.g.,* quantitative limitations on subsidy benefit amounts).

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[3] See, TN/RL/W/33. (This document and other WTO public documents are available on the WTO website at http://docsonline.wto.org.)

[4] See, TN/RL/W/78.

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

Therefore, the U.S. submissions generally addressed the following three issues of subsidy allocation: (1) when to allocate a subsidy over time; (2) how to allocate a subsidy over time; and (3) when allocating a subsidy over time, how to determine the length of time over which the allocation should occur.[6] In its last paper to date on this topic, the United States submitted draft text for possible rules on subsidies allocation.[7]

An additional, practical question that the U.S. proposals on subsidy allocation present is how (and where) any such new rules or guidelines would be incorporated into the Subsidies Agreement. Although one logical place to add such rules is Article 14 (which provides guidelines for calculating the subsidy benefit to the recipient), that Article only pertains to countervailing duty remedies. Recalling that several WTO dispute settlement reports have applied the principles of Article 14 to dispute settlement proceedings under Parts II and III of the Subsidies Agreement, the United States has observed that much, if not all, of Article 14 also seems relevant to Parts II and III of the Subsidies Agreement. The April 2006 U.S. draft text leaves open for further discussion the issue of whether and, if so, how the allocation and expensing rules should be applied to proceedings under Parts II and III of the Subsidies Agreement, in addition to proceedings under Part V.

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

In addition to the latest paper on subsidy allocation, the United States made another submission to the Rules Group in 2006 on the issue of prohibited subsidies.[8] Noting that serious market and trade distortions can result from subsidies other than those currently prohibited by the Subsidies Agreement (*i.e.,* export subsidies and import-substitution subsidies), the United States called upon Members to consider expanding the current prohibition to encompass other subsidies that most typically and directly forestall or impede industry restructuring and rationalization, and which often result in inefficient excess capacity. Among these, the United States suggested considering practices similar to those listed in the now-lapsed “dark amber” provisions of Article 6.1 of the Subsidies Agreement as the “first candidates” for inclusion in an expanded prohibited category of subsidies. Other possible additional candidates

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[6] See, TN/RL/Gen/17, TN/RL/Gen/4, TN/RL/Gen/12

[7] See, TN/RL/Gen/130.

[8] See, TN/RL/Gen/94.

named in the U.S. proposal include government funding of companies in very poor financial health unable to obtain commercial financing.

In addition to proposing the expansion of the prohibited category, the paper also lays out a bold new proposal to address increasing concerns with foreign state-owned and state-controlled enterprises. Questioning the justification for any government investment in the private sector in countries with well-developed capital markets, the paper states that government investment decisions that run counter to the private sector's assessment that a company is not likely to generate a market return should be made in a transparent fashion, closely scrutinized and, as appropriate, curtailed. Accordingly, the paper proposes that there be a requirement that Members notify the WTO Subsidies Committee of government equity investment, including debt-to-equity conversions. Such notifications should describe: (1) the terms of the transaction; (2) how such an investment is consistent with the usual practice of private investors; and (3) potential adverse trade effects. Moreover, additional transparency measures should be considered for all government-controlled companies as well, such that Members can be assured of a consistently commercial, arm's-length relationship between the government-owner and the state-owned enterprise.

The potential importance of this proposal is considerable. It is one of the most far-reaching subsidy-related proposals tabled to date in the Rules negotiations, reinforcing the United States' leadership role in pursuing strong subsidies disciplines under the WTO. The proposed strengthened disciplines would greatly enhance the United States' ability to address, and potentially deter, subsidy-related unfair trade practices confronting U.S. industries. Conditional on the resumption and progress of work in the Rules Group overall, we intend to follow up the January 2006 prohibited subsidies paper with a proposal containing draft text for how such an expanded prohibition could be incorporated into the Subsidies Agreement.

c. Subsidies-Specific Submissions of Other Members

Several other Members also have made important proposals in the Rules Group concerning subsidy-related issues. In many instances, Members have submitted several papers on a single issue. The following table lists other Members' subsidy-related papers for informal discussion submitted to date.[10] Following the table are summaries of those issues actively considered in the plenary or plurilateral sessions of the Rules Group during 2006.

[10]Note: This list does not include those AD-related proposals that might also have relevance for CVD analysis.

Australia	c. Prohibited Export Subsidies (TN/RL/GEN/22) • Prohibited Export Subsidies (TN/RL/GEN/34) • Withdrawal of a Subsidy (TN/RL/GEN/35) • **Prohibited Export Subsidies (TN/RL/GEN/80)** • **Withdrawal of a Subsidy (TN/RL/GEN/97)** • **Withdrawal of a Subsidy (TN/RL/GEN/115)**
Brazil	• Treatment of Government Support for Export Credits and Guarantees under the Agreement on Subsidies and Countervailing Measures (TN/RL/GEN/66) • Serious Prejudice (TN/RL/GEN/81) • De Facto Export Contingency (TN/RL/GEN/88) • **Existence of a Benefit (TN/RL/GEN/101)** • **Further Proposal on Serious Prejudice (TN/RL/GEN/113)**
Canada	• Specificity (TN/RL/GEN/6) • Benefit Pass-Through (TN/RL/GEN/7) • Serious Prejudice (TN/RL/GEN/14) • **Benefit Pass-Through (TN/RL/GEN/86)** • **Amendments to Provisions of the SCM (TN/RL/GEN/112rev.1)**
Chinese Taipei	• **Countervailing Measures (TN/RL/GEN/96)**
European Union	• **Countervailing Measures (TN/RL/GEN/93)** • **Subsidies (TN/RL/GEN/135)**
Egypt, India, Kenya & Pakistan	• **ASCM Articles 27.5 & 27.6 Regarding Export Competitiveness (TN/RL/GEN/136)**

Note: Bolded lettering indicates those papers or issues which were considered by the Rules Group in informal or plurilateral session during 2006.

Turning to those papers which were actively discussed by the Group in 2006, one of Australia's two main proposals is to clarify the definition of a *de facto* export subsidy. As a WTO Member with a small domestic economy, but with a considerable export presence, Australia is concerned that subsidies it provides to its export-oriented industries will be more likely to be found to be contingent in fact on export performance and, therefore, prohibited rather than merely actionable. Australia believes that existing WTO jurisprudence does not provide sufficient clarity or predictability on this matter and is, therefore, proposing changes to ensure that export propensity cannot be the sole or disproportionate consideration in evaluating the evidence of export contingency.

Australia has also submitted several papers on the issue of subsidy withdrawal. Australia believes that the Subsidies Agreement must be clarified to provide Members better guidance with regard to the meaning and scope of the "withdrawal of subsidy"

remedy for prohibited subsidies. Specifically, Australia proposes that the text of Article 4 of the Subsidies Agreement be elaborated to clarify what is required in order to satisfy the test for "withdrawing" a subsidy. Australia's concerns stem directly from the WTO dispute settlement proceedings in the Australian Leather case in which the Panel considered whether the phrase "withdraw the subsidy" could be understood to encompass repayment of the subsidy.

Canada's proposal on benefit pass-through largely reflects Canada's position in the dispute with the United States over softwood lumber. Currently, under the Subsidies Agreement, a subsidy is defined as a financial contribution that provides a benefit. Canada's position is that where the recipient of a financial contribution and the alleged recipient of the resulting benefit are different entities, the investigating authority cannot presume that the benefit "passes through" from one entity to the other. To address this concern, Canada proposes that the Subsidies Agreement be amended to require that a pass-through analysis be conducted in any instance where the recipients of the financial contribution and of the benefit are different entities.

Canada's paper entitled "Proposed Amendments to Certain Provisions of the Agreement on Subsidies and Countervailing Measures" provides textual amendments to the provisions in the Subsidies Agreement regarding "specificity" and "serious prejudice." On specificity, Canada proposes clarifying Article 2.1(c) of the Subsidies Agreement by requiring that a *de facto* specificity analysis involve an assessment of all the factors listed in Article 2.1(c) (*i.e.,* the number of users of a program, whether there is predominant or disproportionate use and the manner in which discretion is exercised in administering the program). Canada also proposes adding a footnote to Article 2, which would require that disproportionality be determined with reference to a relevant objective benchmark, such as the relative importance of recipient industries, in terms of production value, within the jurisdiction of the granting authority.

Regarding serious prejudice, in a September 2004 paper on the issue, Canada had argued for reinstatement of Article 6.1 (the dark amber category), which established a presumption of serious prejudice for certain types of subsidies. In the most recent paper, in addition to reinstating Article 6.1, Canada makes several text-based proposals relating to start-up situations and various calculation issues associated with the dark amber rules.

Beyond the dark amber issue, Canada also proposes various technical changes that would clarify and strengthen the serious prejudice rules currently in place. Specifically, Canada proposes that the descriptions of the concepts of "displacement" or "impeding" provided in Article 6.4 and currently only explicitly applicable to Article 6.3(b) – relating to third country markets – also be applicable to Article 6.3(a), which covers the market of the subsidizing Member. Canada also proposes adding a footnote to Article 7.8 of the Subsidies Agreement which would provide that subsidies fully disbursed prior to the implementation of a dispute settlement ruling be allocated over

the total production of the products "to which the subsidy is properly attributable under generally accepted accounting principles."

Brazil's paper on serious prejudice is in part a response to the Canadian proposal on the same topic. Notably, Brazil supports Canada's earlier proposal to reinstate Article 6.1 (the dark amber category) with certain additions and clarifications. More importantly, Brazil proposes that footnotes 15 and 16, which relate to civil aircraft, be deleted from Article 6.1.

In its paper on the existence of a benefit, Brazil continues to develop its position, building on the WTO's decision in the U.S. Cotton case, that there are important differences regarding a benefit determination between a multilateral dispute under parts II and III of the Subsidies Agreement and a CVD proceeding under Part V. According to Brazil, three general points drawn from U.S. Cotton and Canada Aircraft can be made about benefits under Parts II and III, namely: 1) the determination of a benefit is to be made by a comparison to the commercial marketplace; 2) a benefit will only arise if the recipient has received a "financial contribution" on terms more favorable than those available to the recipient in the market; and 3) a precise calculation of the benefit is not required. Building on these points, Brazil suggests specific language for how loan subsidy benefits will be determined under Parts II and III and, separately, under Part V of the Subsidies Agreement.

Brazil's proposal on export credits appears to be one of the most important subsidies-related issues for Brazil in the Rules Group negotiations. The proposed amendments to items (j) and (k) of Annex I of the Subsidies Agreement seek to further "level the playing field" for government-supported export credits so that developing countries – from Brazil's perspective – are not disadvantaged as compared to developed countries when offering such credits. Brazil's paper also raises the legal relationship between the OECD Arrangement on Officially Supported Export Credits (the Arrangement) and the Subsidies Agreement. Currently, the second paragraph of item (k) provides a "safe harbor" for official export credits provided in accordance with the interest rate provisions of the Arrangement, which is incorporated by reference into the Subsidies Agreement. Brazil argues that this effectively allows OECD Participants to change aspects of the export credit rules under the Subsidies Agreement without the concurrence of all WTO Members.

In its paper on countervailing duties, the EU raises the following issues that have also been discussed in the Rules Group to some extent with respect to the AD Agreement: facts available, sunset reviews, sampling, new shippers ("newcomers"), and "constructive remedies" (*e.g.,* price undertakings). In a second paper entitled "Subsidies," the EU proposes strengthening and expanding the prohibited category of subsidies. The EU first proposes prohibiting "the provision, by virtue of government action, of goods to domestic production on terms and conditions more favorable than those generally available for such goods when destined for export." It appears that, with this provision, the EU is seeking to address what it and other WTO Members see

as the subsidy or subsidy-like effect of the pricing policies of certain countries for natural gas. Under these policies, domestic natural gas prices are regulated at what is widely considered below cost recovery levels, while export prices are markedly higher and generally reflect market prices for petroleum-based products.

The EU also proposes clarifying Article 3.1(b) of the Subsidies Agreement, *i.e.*, the prohibition on subsidies contingent upon the use of domestic over imported goods. The EU's concern is that the current rules arguably require a demonstration of an absolute obligation to use domestic over imported goods -- not just an encouragement or incentive to do so – and may be inadequate to address subsidies simply contingent on some percentage of "local content" or increased domestic "value-added." The EU's last proposal attempts to address the issue of systemic, below-cost financing provided by a government. Specifically, the proposal would prohibit "the provision, by virtue of government action, of finance to a wide range of industries on terms and conditions inadequate to cover the long term operating costs and losses of such finance where this benefits exported goods."

In a jointly-submitted proposal, entitled "Improvement and Clarification in Article 27.5 and 27.6 of the ASCM Regarding Export Competitiveness," Egypt, India, Kenya, and Pakistan propose improving the Subsidies Agreement by making it more difficult for an "Annex VII" country's (*e.g.,* a less developed country's) exports to be determined export competitive under Article 27. (Under existing provisions of the Subsidies Agreement, Annex VII countries can provide export subsidies – which are otherwise prohibited – until a product becomes "export competitive", at which point they normally have eight years to phase the subsidy out.) Currently, Article 27.6 provides that an exported product of an Annex VII country is considered export competitive if exports "have reached a share of at least 3.25 percent in world trade of that product for two consecutive calendar years." The paper proposes that export competitiveness be determined based on two tests; namely: 1) whether exports have reached 3.25 percent for two years; *and* 2) whether the "moving average" of the previous five years was above 3.25 percent for two consecutive years. The proponents also propose a "stop-the-clock" mechanism whereby the "clock" for the phase-out period to eliminate prohibited export subsidies would be stopped if a developing country that had reached export competitiveness subsequently lost it during the phase-out period.

d. Fisheries Subsidies

As part of the Doha mandate, Members have committed to negotiations that "aim to clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries." The United States views these negotiations as a groundbreaking opportunity for the WTO to show that trade liberalization can benefit the environment and contribute to sustainable development as well as address traditional trade concerns. The United States continued to play a major role in advancing the discussion of fisheries subsidies reform in the Rules Group in 2006, working closely with a broad coalition of developed and developing countries,

including Argentina, Australia, Chile, Ecuador, Iceland, New Zealand and Peru (collectively known as the "Friends of Fish").

Although a broad consensus has emerged in favor of stronger disciplines, including a prohibition of the most harmful subsidies (*i.e.*, those that contribute to overfishing and overcapacity), there remains considerable disagreement over the structure of such disciplines, as well as their extent and coverage. The United States and the other Members of the Friends of Fish generally advocate a framework encompassing a broad-based prohibition, with appropriate, well-defined exceptions (referred to as the "top-down" approach). Specifically, the United States supports a prohibition focused on subsidies that contribute to overcapacity and overfishing and consideration of carefully targeted exceptions to allow appropriate flexibility. The United States has also stressed that, to be effective as well as to increase the transparency of existing subsidies, the negotiation of exceptions should be focused on the actual, particular subsidy programs and concerns of Members rather than on broad, open-ended categories of support programs. The United States believes that, grounded in a general prohibition, the top-down approach offers a simple, administrable, enforceable, and realistic structure for strengthened disciplines.

In contrast, some other Members, such as Japan and Korea, advocate a "bottom-up" approach premised on a potentially large number of permitted subsidies and a small number of prohibited subsidies (*i.e.*, those that cause demonstrable adverse resource and trade effects). In response, the United States and the other Friends of Fish have noted that such an approach puts a heavy emphasis on resource effects and introduces concepts (*e.g.*, "properly managed fisheries") that do not fall squarely within the competence and objectives of the WTO. In light of its inherent practical and other difficulties, the United States has suggested that the bottom-up approach could actually lead to a set of disciplines weaker than the current rules.

In April 2006, the United States submitted a paper which proposed draft text to address three technical issues relating to stronger fisheries subsidy disciplines.[11] The first issue related to subsidies for capacity reduction and vessel buyback programs, with the draft text laying out various conditions that should be attached to such programs. The second issue dealt with Committee review, and the draft text proposes various provisions for the Committee's periodic review of the effectiveness of new disciplines on fisheries subsidies, including a role for intergovernmental organizations with fisheries expertise. Regarding the third issue, the paper proposes draft provisions for appropriate involvement of fisheries experts in addressing technical and scientific questions that may arise in dispute settlement proceedings under new fisheries subsidies disciplines.

[11] See, TN/RL/GEN/127.

More generally, with the increasing emphasis on text-based proposal, in 2006, the focus of the fisheries subsidies negotiation shifted back to the broader question of the appropriate overall framework of new disciplines. A variety of proposals were considered which spanned the spectrum between top-down and bottom-up proposals. New Zealand's top-down proposal[12] provides for a very broad prohibition on subsidies to a range of fish-related activities (*e.g.*, harvesting, processing, transport, marketing), with very narrowly defined exceptions for special and differential treatment to developing countries and for certain kinds of subsidies that do not contribute to overcapacity or overfishing (subsidies to, *e.g.*, general infrastructure, vessel decommissioning, fisheries management, conservation and research). The bottom-up proposal from Japan, Korea and Chinese Taipei, on the other hand, prohibits only a limited number of subsidies, and only under limited circumstances (*e.g.*, where the subsidizing Member does not maintain adequate fishery management, and where the subsidy involves illegal, unreported and unregulated fishing.)[13]

Similarly, the EU submitted a less-than-ambitious proposal for stronger disciplines only on subsidies that clearly support overcapacity, with broad, poorly defined exceptions for social and environmental reasons and for developing countries.[14] The EU's proposal sets out some notification requirements for permitted subsidies, as well as a mechanism for review of such programs by the Permanent Group of Experts (PGE) (see section D.5., below, discussing the role of the PGE).

A number of developing countries have also submitted framework proposals with a particular focus on special and differential treatment provisions under any strengthened disciplines. Brazil's comprehensive textual proposal for an overall framework for new fisheries subsidies disciplines, including provisions for special and differential (S&D) treatment, has been the focus of a considerable amount of discussion within the Group, and has been revised several times.[15] Argentina and India also submitted proposals on the issue of stronger fishery disciplines and S&D treatment.[16] These followed proposals made in prior years by other developing countries, including a group comprised of "small, vulnerable coastal states."[17]

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[12] See, TN/RL/GEN/100 and TN/RL/GEN/141.

[13] See, TN/RL/GEN/114Rev.1

[14] See, TN/RL/GEN/134

[15] See, TN/RL/GEN/79Rev.3

[16] See, TN/RL/W/203, TN/RL/GEN/79Rev.3, TN/RL/GEN/138,

[17] See, TN/RL/GEN/57Rev2.

Many of the framework proposals from developed and developing countries alike have attempted to deal with the difficult issues of small scale fishing, artisanal fishing, de minimis rules and access fees, and how these may or may not be part of any S&D treatment provisions. These issues are very complex, however, and a consensus among the Rules Group has not yet emerged. Some concepts, such as "small scale" or "artisanal," do not have a single, commonly accepted definition, and can involve areas of expertise in fishery resources that are traditionally outside the competence of the WTO. Nevertheless, the United States and other Friends of Fish recognize the Doha Mandate to "clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries," and remain committed to working with all Members to address the practical problems that developing countries may face in implementing stronger disciplines on fisheries subsidies.

d. Agriculture Subsidies

At the Fourth WTO Ministerial Conference in Doha, Members agreed to an ambitious mandate for agriculture, including "substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support." This mandate calling for significant results in all three areas (the so-called "pillars") was augmented with specific provisions for agriculture in the framework agreed upon by the General Council on August 1, 2004 and at the Hong Kong Ministerial Conference in December 2005.

The United States has long advocated fundamental reform of all trade-distorting measures by all WTO Members. In 2002, the United States made specific proposals to phase-out all tariffs, trade-distorting domestic support, and export subsidies in the Doha negotiations. The United States submitted a comprehensive and ambitious proposal in October 2005, consistent with the 2002 U.S. proposal and the 2004 WTO framework, calling for substantial reductions in tariffs and trade-distorting domestic support in two phases. Pursuant to this proposal and the agreed framework, the higher tariffs and Members with higher subsidy levels would be subject to deeper cuts phased-in over a five-year period for developed country Members, with developing country Members taking lesser cuts and more time to implement these cuts. In the second five-year phase (immediately following the first), all tariffs and trade-distorting domestic support would be eliminated. Under the U.S. proposal, export subsidies would be eliminated within the first phase of reform, with parallel commitments undertaken on export state trading enterprises, export credits, and food aid programs.

While numbers and formulas for making the cuts were on the table, the differences between Members were too large to be resolved at the Hong Kong Ministerial Conference. Substantive discussions on agriculture at Hong Kong focused on setting an end date for export subsidies, where Members agreed to an end date for export subsidies in 2013, with the further commitment that the substantial part of the elimination would be completed by 2010. Members further narrowed some of their key differences in other areas, including a commitment to a sectoral negotiation on cotton

where trade-distorting domestic support would be cut deeper and more quickly than for other commodities (with the actual numbers subject to negotiation) and a commitment that developed country Members would eliminate tariffs on cotton exports from the least-developed country Members.

Negotiations in 2006 focused on specifying how far and how fast tariffs and trade-distorting domestic support would be reduced, and how to phase in the elimination of export subsidies. Major differences existed between Members, such as the United States, that called for substantial market opening through deep tariff cuts and large tariff-rate quotas for sensitive products that would avoid deep tariff cuts, and other Members that called for limited actions. Of particular difficulty was reaching agreement on treatment of import sensitive products in developed country Members, and provisions for developing country Members for import of sensitive products and products with special relationships to food security, rural development, and rural livelihoods. In addition, negotiations focused on the depth of cuts for trade-distorting domestic support, with subsidy programs in the United States and the EU attracting particular attention. Despite intensive negotiations and additional special negotiating sessions among WTO Members, agreement was not reached, and in July the Director-General of the WTO formally suspended the negotiations. For the remainder of the year, negotiators met informally to explore ideas and potential scenarios that could lead to breaking the impasse and putting the negotiations on a path to a result consistent with the Doha mandate.

In 2007, the United States will continue the informal work with key trading partners that began in 2006 to try to identify approaches for reviving the negotiations in a manner that would deliver on the Doha mandate. In these discussions, the United States will work to achieve a high level of ambition in all three pillars: market access, export competition, and trade-distorting domestic support.

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

In 2006, the United States worked to address concerns related to the rapidly changing trade situation in the global steel sector, continuing its work at the OECD, the NASTC and beginning a new steel dialogue with China under the JCCT.

The United States remained engaged with the OECD Secretariat and governments of other steel-producing economies to take up policy issues affecting the global steel industry. These included issues related to capacity expansion, government subsidies in the steel sector, the environmental impact of steelmaking technologies and raw materials issues. The United States supported efforts by the OECD Secretariat to reach out to developing steelmaking economies, including the organization of a major steel conference held in May 2006 in New Delhi, India, jointly hosted by the OECD, the Government of India and the International Iron and Steel Institute, a global steel industry association.

The explosive growth of China's steel production emerged as a major development for the United States and other global steel producers in 2006. Reflecting concerns that the growth of China's largely state-owned industry was not responding to a slowdown in demand, in December 2005 the United States obtained China's agreement to initiate a cooperative dialogue under the auspices of the JCCT, led by Commerce and USTR on the U.S. side, and by the Ministry of Commerce on the Chinese side. This dialogue represents an effort to increase Chinese government and industry understanding of market-oriented behavior and the problems that subsidies and other government intervention in the steel sector can cause in world steel markets. Two meetings of the dialogue took place in 2006 and have included participation by industry representatives from both countries as well as the National Development and Reform Commission, the Chinese agency responsible for steel industrial policies.

The governments and steel industries of North America have continued their wide-ranging work to seek common policy approaches to enhance the competitiveness of North American steel producers. To implement the "North American Steel Strategy" under the 2005 Security and Prosperity Partnership (SPP) initiative by the countries' three leaders, the NASTC has worked to coordinate North American positions on issues of importance to steel in multilateral fora, including the OECD Steel Committee and the WTO Rules Negotiations. Within the mandate of the NASTC, the three governments and steel industries have been tracking developments in certain steel-producing countries to identify and address, as appropriate, distortions in the global steel market. In a joint statement submitted to the OECD Steel Committee, the three governments highlighted their concerns with these developments and called upon all steel-producing countries to take steps to address the adverse effects of government intervention in the global steel sector and to facilitate the closure of non-viable capacity. The United States also continued working with the governments of Canada and Mexico to enhance compatibility of the steel import monitoring systems maintained by all three NAFTA countries.

The United States also continues to raise specific concerns with other countries bilaterally, at the OECD and in WTO accession negotiations, about steel policies that contribute to excess capacity and production, including subsidies, border measures on steel and steelmaking raw materials, and other trade-distorting practices.

MONITORING AND ENFORCEMENT

A. ADVOCACY EFFORTS

1. Counseling U.S. Industry

USTR and IA staff regularly work with U.S. companies concerned with the subsidization of foreign competitors. The goal is to resolve problems through a combination of informal and formal contacts. However, where appropriate, the United

States will also advise U.S. companies of other options for action, such as a CVD investigation, WTO dispute settlement or an action taken under Section 301 of the Trade Act of 1974.

In 2006, a number of U.S. companies sought assistance in this regard. USTR and IA worked closely with the affected companies to collect information concerning the potential subsidies and to determine how their commercial interests may have been harmed. While companies facing subsidized competition can usually provide good information as to the financial health of their industry, assistance is often needed to obtain additional information regarding the alleged subsidy in question. In these instances, USTR and IA conduct significant additional research to determine the legal framework under which the foreign government is offering the assistance and whether other U.S. exporters have been facing similar problems. USTR and IA staff also draw upon additional internal and external sources to develop information concerning potentially harmful foreign subsidies. These include Commerce/ITA offices with country and industry specialists that routinely collect information on regional or sector-specific subsidies. If appropriate, U.S. embassies in the relevant foreign countries are contacted for additional "on the ground" information they may be able to provide. On occasion it has also been useful to contact other governments to learn whether similar complaints about the same third-country subsidy have been identified by their exporters.

Working with an interagency team, USTR and IA staff then evaluate the information and determine the most effective way to proceed. As noted above, it is often advantageous to pursue resolution of these problems through a combination of informal and formal contacts. For example, raising the matter with the foreign government authorities through informal contacts, formal bilateral meetings or through discussions in the WTO Subsidies Committee may produce more expeditious and practical solutions to the problem than resorting to WTO dispute settlement or the filing of a CVD petition. These contacts may also lead to additional information about the practice which, in turn, can affect the decision concerning the appropriate measures to take. However, if these efforts fail to resolve the issue, bringing a formal dispute settlement action in the WTO always remains a viable option.

During 2006, USTR and Commerce continued to work with a broad array of U.S. industries and companies that complained about unfair foreign government subsidy practices in a wide range of countries. These activities included ongoing work on behalf of the U.S. textile, steel, aerospace, paper, automobile, and biotechnology industries. The subsidy practices examined included those maintained by the governments of China, Korea, Canada, the European Union and its Member States, Malaysia, Brazil, Chinese Taipei, India, Russia, Ukraine and Japan.

2. Outreach Efforts

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

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

USTR and IA staff work closely with the other U.S. Government agencies, including the Department of State and the U.S. Department of Agriculture, to involve foreign service economic and agriculture officers in subsidies enforcement activities.[18] To this end, USTR and IA personnel train state foreign service officers on how to identify and evaluate foreign subsidy practices. Cooperation of this type occurs not only when initiated by IA or USTR, but on an ongoing basis whereby state foreign service officers develop and share information with Commerce, USTR and the interagency team concerning foreign government subsidy practices and the administration of foreign

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

governments' unfair trade laws.[19] This type of collaboration among government agencies is critically important to help exercise effectively U.S. rights under the Subsidies Agreement.

IA also arranges and participates in training sessions for foreign government officials. A major focus of these programs is a detailed discussion of the Subsidies Agreement. In 2006, IA staff worked with officials from a number of countries such as Egypt; Bosnia; Pakistan and the European Communities, stressing procedural issues, calculation methodologies, and the importance of transparency. The training activities form part of a comprehensive program to strengthen ties between foreign officials and their U.S. counterparts, and to help ensure that the administration of trade remedy laws by other WTO Members is consistent with their international obligations.

3. Monitoring Subsidy Practices Worldwide

In 2006, USTR and IA staff expanded their efforts to monitor market- and trade-distorting practices by governments worldwide, including the provision by governments of harmful subsidies. In particular, IA staff implemented enhanced protocols for identifying, researching and evaluating subsidy programs and other potential unfair trade practices. This work, which is conducted by experienced analysts in IA, involves daily searches of worldwide business journals, periodicals, news publications, as well as online resources maintained by governments, industries and international organizations. Analysts fluent in a variety of foreign languages, e.g., Chinese, French and Spanish, also conduct research in their language of expertise. Information is obtained from U.S. embassies overseas through cable reports and direct inquiries by USTR and IA staff for in-depth country-related research. IA research activities are also aided by ongoing relationships with U.S. industry contacts, both in the United States and overseas.

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

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

the WTO (which maintains databases of Members' CVD actions, and their subsidy notifications to the WTO), the Canadian and Mexican government trade agencies and the NAFTA secretariat. The website is updated frequently to provide the most recently available information to the public in a timely manner.

B. CHINA

1. World Trade Organization – Transitional Review Mechanism (TRM)

Paragraph 18 of Part I of the Protocol of Accession of the People's Republic of China to the WTO provides that all subsidiary bodies, including the Subsidies Committee, "which have a mandate covering China's commitments under the WTO Agreement or [the] Protocol shall, within one year after accession . . . review, as appropriate to their mandate, the implementation by China of the WTO Agreement and of the related provisions of [the] Protocol." Paragraph 18 further states that such reviews shall be conducted on an annual basis for eight years, with a final review occurring by the tenth year after accession. In October 2006, the United States took part in the fifth annual transitional review with respect to China's implementation of its WTO obligations.

Following increasing pressure from the United States and other WTO Members, China finally submitted its long-overdue subsidies notification to the WTO's Subsidies Committee in April 2006. Although the notification is lengthy, with over 70 subsidy programs reported, it is also notably incomplete. For example, China failed to notify any subsidies provided by its state-owned banks or by provincial and local government authorities. In addition, while China notified several subsidies that appear to be prohibited, it did so without making any commitment to withdraw them, and it failed to notify other subsidies that appear to be prohibited. The United States has devoted significant time and resources to monitoring and analyzing China's subsidy practices.[20] These efforts helped to identify significant omissions in China's subsidy notification. In accordance with Subsidies Committee procedures, the United States submitted extensive written questions and comments on China's subsidies notification in July 2006, as did several other WTO Members, including the EU, Japan, Canada, Mexico, Australia and Turkey. China has not yet responded in writing to these submissions. During the October transitional review before the Subsidies Committee, the United

[20] In the course of the TRM, the United States also raised China's continued failure to submit written answers to the United States' Article 25.8 questions posed to it two years ago (October 2004). Article 25.8 of the Subsidies Agreement authorizes any WTO Member to request information on the nature and extent of any subsidy granted or maintained by another Member. Under Article 25.9 of the Agreement, China is obligated to provide a written, comprehensive response to the U.S. questions. Although China's subsidy notification touched on some of the issues raised in questions presented by the United States, to date China has not provided written responses to the October 2004 questions submitted by the United States.

States reiterated its concerns about China's subsidies notifications and urged China to withdraw its prohibited subsidies without delay.[21]

The United States began seeking changes to China's subsidies practices immediately after China submitted its subsidies notification in April 2006. Through a series of bilateral meetings in Beijing, including high-level meetings, the United States made clear that China needed to withdraw both the prohibited subsidies that it had notified and several additional prohibited subsidies that it had not notified. The subsidies at issue benefit a wide range of industries in China and include both export subsidies, which make it more difficult for U.S. manufacturers to compete against Chinese manufacturers in the U.S. market and third-country markets, and import substitution subsidies, which make it more difficult for U.S. manufacturers to export their products to China. Although the exchanges helped to clarify concerns and certain information, China has been unwilling to commit to the immediate withdrawal of the subsidies in question. The United States continues to press China on this issue and will take further action to end these prohibited subsidies.

The United States intends to step up its dialogue with China about its subsidies policies and programs. In the July 2005 U.S.-China Joint Commission on Commerce and Trade (JCCT) meeting, the Chinese government agreed to an "intensified" process of discussions in SIWG meetings, including a direct discussion of Chinese subsidies. (See JCCT discussion, below.)

2. JCCT - Structural Issues Working Group (SIWG)

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

In the case of China, one avenue to help ensure that the playing field is made more level is to encourage China's ongoing structural reforms, which are intended to create a market economy. At the same time, China's treatment as a non-market economy under U.S. antidumping law is of substantial concern and importance to the Chinese government. In order to better understand China's reforms to date and various structural and operational aspects of China's economy, as well as discuss issues that relate to China's desire for market economy status under the U.S. antidumping law,

[21] See, also, 2006 Report to Congress on China's WTO Compliance, United States Trade Representative, December 11, 2006, pp. 41-43

China and the United States agreed during the April 2004 JCCT meetings to the establishment of a new working group, the SIWG, to be jointly chaired by Commerce's Assistant Secretary for Import Administration and the Assistant U.S. Trade Representative for China Affairs on the U.S. side and the Director General of the Bureau of Fair Trade from China's Ministry of Commerce (MOFCOM) on the Chinese side.

The United States attaches great importance to the SIWG. It provides a forum for the U.S. and Chinese governments to explore and discuss China's economy and its ongoing economic reform program, pragmatically address concerns about trade- and market-distorting practices that might otherwise lead to bilateral trade frictions, and consider the Government of China's concerns about China's nonmarket economy (NME) status under U.S. antidumping law.[22] The working group has met three times since its launch in July 2004, with both sides including in their delegations experts from a variety of agencies responsible for the broad range of structural/institutional issues and economic reforms/policies under discussion. During the July 2005 meeting of the JCCT, China and the United States agreed to intensify the SIWG process to provide greater opportunity to explore with China its economic policies and reforms at a more technical level. In addition, the United States made it a priority to directly address subsidies in the SIWG and obtained Chinese government agreement to do so.

In the inaugural meeting of the U.S.-China Strategic Economic Dialogue in December, both China and the United States agreed to invigorate discussion under the JCCT of structural issues/market economy status. The United States views this mandate and the high degree of interest in the Strategic Economic Dialogue as a revival of China's commitment to the broad agenda of the SIWG, and its intention to push for real progress. To that end, the United States has been working with China to schedule a next meeting of the working group, which we now expect to take place in the Spring of 2007.

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

3. Application of Countervailing Duty Law

Twenty years have passed since the landmark decision in *Georgetown Steel Corp. v. United States*, 801 F.2d 1308 (Fed. Cir. 1986) ("*Georgetown Steel*"), which affirmed Commerce's policy at the time of not applying the CVD law to countries classified as NMEs for antidumping purposes. Most NMEs have changed significantly since then, and the question has arisen of whether or to what extent the logic of *Georgetown Steel* still applies today. Some in the U.S. industry point with increasing alarm at what they believe is growing evidence of the broad scope and pervasive nature of NME government subsidy practices and their impact on trade and market access. Various non-governmental organizations have also noted that NME government subsidies continue to frustrate much-needed industrial restructuring and efficient resource allocation, and many WTO Members are becoming increasingly aware of NME government subsidy practices as a result of bilateral and multilateral discussions in the WTO, OECD and other fora. As a result, WTO Members have expressed concern and reiterated their requests that NME governments make their subsidy regimes more transparent and consistent with their international obligations, so that the nature and scope of NME government subsidy practices can be better understood and their trade effects meaningfully assessed.

In October 2006, a petition was filed with Commerce requesting the initiation of a CVD investigation, based on allegations of injurious subsidized imports of coated free sheet (CFS) paper, from China. The petition notes that Commerce currently does not apply the U.S. CVD law to nonmarket economies such as China, and requests a change in that policy. On November 21, 2006, Commerce announced its decision to initiate a CVD investigation on imports of CFS paper from China. In 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 of the applicability of the CVD law to NME countries, in particular, China. Commerce intends to consider and address this issue in the context of the CFS paper investigation. To this end, Commerce has issued a Federal Register notice, requesting public comment on the issue of the application of the CVD law to imports from China. As of January 16, 2007, Commerce received comments from over 50 parties, all of which will be carefully reviewed during the course of the investigation.

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

1. European Union Support for Airbus

For many years, the United States has had serious concerns about the continued EU subsidization of Airbus, a company with more than a 50 percent share of the world market for large civil aircraft ("LCA"). The subsidies have taken many forms,

including "launch aid," which Airbus uses to launch new models of aircraft; grants for Airbus infrastructure; forgiveness of debt; and subsidies to underwrite Airbus' research and development costs.

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

The WTO consultations failed to resolve the U.S. concerns, and a renewed effort to negotiate a solution ended without success in April, 2005. Therefore, on May 31, 2005, the United States filed a WTO panel request. The EU filed a WTO panel request on the same day with respect to alleged U.S. federal, state and local government subsidies to Boeing. The WTO established the panel on July 20, 2005, and panel proceedings are currently ongoing. The United States filed its initial brief on November 15, 2006. The EU rebuttal brief is due February 9, 2007.

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

2. United States Support for Upland Cotton

On September 27, 2002, Brazil requested WTO consultations pursuant to Articles 4.1, 7.1 and 30 of the Agreement on Subsidies and Countervailing Measures, Article 19 of the Agreement on Agriculture, Article XXII of the General Agreement on Tariffs and Trade 1994, and Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes. On February 6, 2003, Brazil requested the establishment of a panel. The Dispute Settlement Body established the panel on March 18, 2003.

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

prohibited export subsidies and Step 2 payments to domestic users are prohibited import substitution subsidies because they were contingent upon the purchase of U.S. cotton.

On October 18, 2004, the United States filed a notice of appeal with the Appellate Body; Brazil then cross-appealed. The Appellate Body circulated its report on March 3, 2005. The Appellate Body upheld the panel's findings appealed by the United States. The Appellate Body also rejected or declined to rule on most of Brazil's appeal issues. On March 21, 2005, the DSB adopted the panel and Appellate Body reports and, on April 20, 2005, the United States advised the DSB that it intends to bring its measures into compliance.

On June 30, 2005, the United States announced certain administrative changes relating to its export credit guarantee programs. Further, on July 5, 2005, the United States proposed legislation relating to the export credit guarantee and Step 2 programs. On the same day, Brazil requested authorization to impose countermeasures and suspend concessions in the amount of $3 billion in connection with the "prohibited subsidy" findings. On July 14, 2005, the United States objected to the request, thereby referring the matter to arbitration. On August 17, 2005, the United States and Brazil agreed to suspend the arbitration. On October 6, 2005, Brazil made a separate request for authorization to impose countermeasures and suspend concessions in the amount of $1.04 billion per year in connection with the "serious prejudice" findings. The United States objected to Brazil's request on October 17, 2005, and that matter was also referred to arbitration. Thereafter, on November 21, 2005, the United States and Brazil jointly requested suspension of this second arbitration.

On September 28, 2006, the Dispute Settlement Body established an Article 21.5 (compliance) panel, at Brazil's request, to review U.S. compliance with the rulings in the dispute. Brazil has argued that the United States remains out of compliance with both the prohibited subsidy findings and the actionable subsidy findings. The compliance panel is scheduled to issue its report to the parties in June 2007.

3. Canada's Challenge of the CVD Investigation of Canadian Lumber

On May 3, 2002, Canada requested WTO consultations with the United States regarding Commerce's final CVD determination concerning certain softwood lumber from Canada. Among other things, Canada challenged the evidence upon which the investigation was initiated, claimed that Commerce imposed countervailing duties against programs and policies that are not subsides and are not "specific" within the meaning of the Subsidies Agreement, and that Commerce failed to conduct its investigation properly. Consultations were held on June 18, 2002, and a panel was established at Canada's request on October 1, 2002.

In its report, circulated on August 29, 2003, the panel found that the United States acted consistently with the Subsidies Agreement and GATT 1994 in determining

that the programs at issue provided a financial contribution and that those programs were "specific" within the meaning of the Subsidies Agreement. It also found, however, that the United States had acted inconsistently with the Subsidies Agreement when it rejected private timber prices in Canada as the benchmark to determine whether – and to what extent – Canada was subsidizing lumber companies by providing low-cost timber. (Commerce had used U.S. prices as the basis for the benchmark, rejecting Canadian private prices because they were distorted by the government's dominance in the timber market.) The panel also found that the United States had improperly failed to conduct a "pass-through" analysis to determine whether subsidies granted to one producer were passed through to other producers. The United States appealed these issues to the WTO Appellate Body on October 21, 2003, and Canada appealed the "financial contribution" issue on November 5, 2003.

On January 19, 2004, the WTO Appellate Body issued a report in which it reversed the panel's unfavorable finding with respect to the rejection of Canadian prices as a benchmark; upheld the panel's favorable finding that the provincial governments' provision of low-cost timber to lumber producers constituted a "financial contribution" under the Subsidies Agreement; and reversed the panel's unfavorable finding that Commerce should have conducted a "pass-through" analysis to determine whether subsidies granted to one lumber company were passed through to other lumber companies through the sale of subsidized lumber. The Appellate Body's only finding against the United States was that Commerce should have conducted such a pass-through analysis with respect to the sale of *logs* from harvester/sawmills to unrelated sawmills.

On March 5, 2004, the United States notified the DSB of its intention to implement the findings of the Appellate Body. The Government of Canada and the United States agreed that 10 months was a reasonable period of time for implementation. On November 9, 2004, pursuant to section 129 of the Uruguay Round Agreements Act, USTR requested that Commerce issue by December 17, 2004, a revised determination not inconsistent with the findings of the Appellate Body. On December 6, 2004, Commerce issued its section 129 determination reflecting its analysis of Canada's claims for an adjustment to the subsidy rate to account for "arm's-length" sales of logs (from provincial government land) in which some or all of the stumpage subsidy benefit did not "pass through" to the purchasing sawmills. On December 10, 2004, USTR, after consultations with Commerce and congressional committees, directed Commerce to implement the revised determination. The notice of implementation was published in the Federal Register on December 16, 2004.

On December 30, 2004, Canada requested formation of an Article 21.5 "compliance" panel to consider the consistency of Commerce's "pass-through" implementation decision. Canada also sought authority to suspend WTO concessions pursuant to Article 22.2 of the DSU; however, that action was stayed to permit the Article 21.5 challenge to proceed. In April 2005, the Article 21.5 panel held a hearing on Canada's claim. Thereafter, on August 1, 2005, the panel issued its decision finding

that Commerce's implementation was inconsistent with its WTO obligations. In making its decision, the Article 21.5 panel extended its jurisdiction to encompass the results of a subsequent review. The United States appealed that aspect of the Article 21.5 panel decision to the Appellate Body. On December 5, 2005, the Appellate Body upheld the Panel's exercise of jurisdiction over the subsequent review. On December 20, 2005, the DSB adopted the reports. As a consequence of the entry into force of the 2006 Softwood Lumber Agreement (see below), Canada's Article 22.2 request for concessions was withdrawn.

4. Canada - U.S. Softwood Lumber Agreement

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

Under the terms of the Agreement, when lumber prices decline to a certain level, Canadian exporting provinces can choose either to collect an export tax that ranges from 5 to 15 percent as prices fall, or to collect lower export taxes in return for export volume limits. If softwood lumber prices rise to $355 per thousand board feet, imports from Canada are unrestricted. Certain softwood lumber products are excluded from the border measure: (1) softwood lumber made from logs harvested in the Maritimes provinces (New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador); (2) softwood lumber made from logs harvested in the Yukon, Northwest Territories, or Nunavut; and (3) softwood lumber manufactured by one of 32 named companies, primarily located in Quebec (largely "border mills" that source most of their logs from Maine). The Agreement also includes provisions to address potential import surges from Canada, provide for effective dispute settlement, and discipline future trade cases.

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

5. Korea's Challenge to the CVD Investigation of DRAMs from Korea

Following final affirmative determinations by both Commerce and the ITC, on August 11, 2003, Commerce published a CVD order on dynamic random access memory semiconductors ("DRAMS") from Korea. The order imposed cash deposits of 44.29 percent on imports of DRAMS produced by Hynix. This cash deposit rate was based largely on Commerce's finding that the Korean Government had provided, or had "entrusted or directed," private bodies to provide massive subsidies to Hynix in order to save it from going out of business. Commerce excluded the other major Korean producer, Samsung, from the order because Commerce found that the subsidies Samsung received were at *de minimis* levels.

On June 30, 2003, Korea instituted dispute settlement proceedings in the WTO. On January 23, 2004, a panel was established to review Commerce's CVD determination as well as the ITC's injury determination. On February 21, 2005, the panel circulated its report in which it decided that Commerce's CVD order, and more specifically its finding of entrustment or direction, was not consistent with WTO rules. With respect to Korea's challenge to the ITC determination of injury, with one exception the panel agreed with the United States on all of the issues. The exception involved one minor aspect of the injury determination where the panel found that the ITC had not adequately explained its analysis. The United States did not appeal this panel finding.

The United States appealed the panel's findings with respect to Commerce's CVD determination to the WTO Appellate Body. The Appellate Body issued its report on June 27, 2005. The Appellate Body agreed with the United States that the panel committed the following key errors: (1) the panel failed to consider the evidence of entrustment or direction in its totality, as Commerce had done, requiring instead that individual pieces of evidence in themselves establish entrustment or direction; (2) the panel declined to consider evidence on the Commerce administrative record but not cited by Commerce in its published determination; (3) the panel failed to make an

objective assessment of the matter within the meaning of Article 11 of the DSU by finding, notwithstanding the absence of supporting evidence in Commerce's record, that certain Hynix creditors had invoked mediation provisions of Korean law; and (4) the panel essentially applied a *de novo* review, thereby failing to comply with Article 11 of the DSU. As a result, the Appellate Body reversed the panel's finding that Commerce's determination of Korean Government entrustment or direction was inconsistent with the Subsidies Agreement. The Appellate Body also reversed other panel findings that were based on the panel's finding concerning entrustment or direction. The Appellate Body also modified the panel's interpretation of the phrase "entrusts or directs" as used in Article 1 of the Subsidies Agreement.

In addition, having reversed the panel's findings, the Appellate Body declined to "complete the analysis" of the panel that had been based upon an improper interpretation and application of the provisions of the Subsidies Agreement. As a result, the original Commerce determination was upheld. The DSB adopted the panel and Appellate Body reports on July 20, 2005. The United States and Korea subsequently agreed that the reasonable period of time for the United States to implement the adverse panel ruling with respect to the ITC's injury determination will expire on March 8, 2006.

On February 13, 2006, the ITC issued a determination under section 129 of the URAA to render its injury determination not inconsistent with the panel's findings. In the section 129 determination, the ITC continued to determine that the domestic DRAMS industry was materially injured by reason of subsidized imports from Korea. After consultation with the appropriate congressional committees, USTR notified Commerce in a letter dated March 1, 2006, of the ITC's determination and requested that it be implemented. Accordingly, on March 8, 2006, Commerce published an amendment to the CVD order on DRAMS from Korea in the *Federal Register* consistent with the ITC's section 129 determination.

6. European Communities' Challenge to Commerce's "Privatization" Methodology - Spain and United Kingdom

In 2001, the European Communities (EC) challenged Commerce's findings in the 2000 sunset reviews of the CVD orders on certain steel products from Spain and the United Kingdom, as well as the findings in ten other CVD cases involving imports of European steel products. Specifically, the EC argued that Commerce's methodology for analyzing the impact of the privatization of formerly state-owned companies on any pre-privatization subsidies they received was inconsistent with U.S. obligations under the Subsidies Agreement. A WTO panel and the Appellate Body agreed and overturned Commerce's privatization methodology.

In June 2003, in response to a request from USTR that Commerce correct its methodology to conform with the WTO dispute settlement findings, Commerce adopted and applied a new privatization methodology to the facts of the 12 disputed cases. Commerce's new methodology focused essentially on whether a privatization was conducted at arm's length and for fair market value. In the Spanish and UK cases, Commerce found that, even assuming that the Spanish and UK steel privatizations occurred at arm's length and at fair market value, countervailable subsidization would likely continue or recur in light of certain other subsidies unaffected by privatization, and thus the CVD orders should remain in place.

Commerce's section 129 findings in the UK and Spanish cases, as well as in a third sunset review on corrosion resistant steel from France, were again challenged by the EC. In an August 17, 2005 decision, a WTO Article 21.5 panel upheld Commerce's finding in the French case, but found that Commerce failed to comply with the express language of the original panel and Appellate Body reports in that it did not examine the privatizations in the UK and Spanish cases. Moreover, regarding the UK case, the compliance panel faulted Commerce's decision not to consider evidence, submitted for the first time during the implementation proceeding, regarding another, private UK company.

Noting that the United States had been upheld on the more important, substantive findings at issue in the French case, the United States subsequently agreed to the adoption of the compliance panel's findings regarding the UK and Spanish cases. USTR then requested that Commerce bring these measures into conformity with the compliance panel's findings. Accordingly, in further proceedings pursuant to section 129 Commerce re-examined the UK and Spanish steel privatizations, as well as a sale of a private UK steel producer, to determine what impact, if any, those transactions had on the likelihood of continued or recurring countervailable subsidization under those orders. On May 26, 2006, Commerce issued its revised section 129 determinations of the CVD orders with regard to the UK and Spanish cases, finding that the evidence on the record did not support a conclusion that the privatizations were conducted at arm's length or for fair market value.

Separately, as a result of the 2005 sunset review, Commerce revoked the UK order in October 2006, and on December 14, 2006, the ITC announced its negative determination with respect to Spain.

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

On September 16, 2005, the Canada Border Services Agency (CBSA) initiated antidumping and CVD investigations on grain corn originating in or exported from the United States. On November 15, 2005, the Canadian International Trade Tribunal (CITT) announced a preliminary affirmative injury determination with respect to unprocessed grain corn and terminated the investigations with respect to processed

grain corn. On December 15, 2005, the CBSA preliminarily determined that three U.S. Government programs – the Direct and Countercyclical Payment Program, the Nonrecourse Marketing Assistance Loans and Loan Deficiency Payments, and Federal Crop Insurance Programs – provided countervailable subsidies to U.S. corn growers and imposed a preliminary countervailing duty of US$1.07 per bushel of corn imported into Canada.

Throughout the CVD investigation, USTR, Commerce and the Department of Agriculture strongly defended the interests of the U.S. corn industry. These efforts included providing factual information to the Canadian authorities, providing written arguments to the CBSA and CITT, and participating in verification meetings in Washington on February 15 and 16, 2006. In addition, on March 17, 2006, the United States requested WTO dispute settlement consultations with Canada with respect to the CITT's preliminary injury determination. Those consultations were held in Ottawa on April 6, 2006.

On March 15, 2006, CBSA issued a final affirmative determination of subsidization, reducing the amount of the final subsidy found to exist to US$0.45 per bushel. On April 18, 2006, however, the CITT made a final determination of no injury from the subsidized imports. Accordingly, the investigations were terminated and all preliminary duties were refunded.

On June 7, 2006, three Canadian provincial corn producer associations appealed the final CITT no-injury determination to Canada's Federal Court of Appeal. The United States submitted a brief to the court on December 4, 2006; oral argument and a final decision are expected in 2007. In addition, several Canadian corn importers requested review of certain aspects of the final CBSA subsidy determination by a binational panel under Chapter 19 of the North American Free Trade Agreement. USTR, on behalf of the U.S. Government, submitted a complaint in this proceeding on May 31, 2006, alleging errors with respect to the CBSA's decision not to conduct a "pass-through" analysis with respect to certain payments made to persons other than corn producers. By consent of all parties, the Chapter 19 proceeding has been stayed pending the outcome of the appeal of the CITT determination.

On January 8, 2007, Canada requested dispute settlement consultations with the United States alleging that support to U.S. corn producers has caused and threatens to cause serious prejudice to the interests of Canada, specifically through price suppression in the Canadian corn market. The allegation included programs at issue in the 2001 and 2006 Canadian CVD investigations, including direct payments, counter-cyclical payments, and marketing loan programs under the 2002 Farm Bill; production flexibility contracts and marketing loan programs under the 1996 Farm Bill; market loss assistance payments under a number of pre-2002 statutes; and export credit guarantee programs. Canada also alleged that U.S. export credit guarantee programs for corn and all unscheduled commodities constitute prohibited export subsidies and that U.S. government support for all agricultural products resulted in a breach of the U.S.

scheduled cap on its Aggregate Measure of Support (AMS) under the Agreement on Agriculture.

D. WTO SUBSIDIES COMMITTEE

The Subsidies Committee's agenda in 2006 included its routine activities concerned with reviewing and clarifying the consistency of WTO Members' domestic laws, regulations and actions with Agreement requirements. During the fall meeting, the Committee undertook its fifth annual transitional review with respect to China's implementation of the Agreement (see, *Transitional Review Mechanism* section above). The Committee, and the United States, continued to accord special attention to the general matter of subsidy notifications made to and considered by the Subsidies Committee. Of particular note, in April 2006 China submitted its first subsidy notification to the WTO, which was reviewed at the Committee's Fall meeting (see, *Application of the Countervailing Duty Law* section above). Other issues addressed in the course of the year included: the examination of the export subsidy program extension requests of certain developing countries, the review of Member's semi-annual reports, the calculation update of the per capita GNP threshold in Annex VII of the Agreement, and consideration of an appointment to the Permanent Group of Experts.

1. Subsidy Notifications

Subsidy notification and surveillance is one means by which the Subsidies Committee and its Members seek to ensure adherence to the disciplines of the Subsidies Agreement. In keeping with the objectives and directives expressed in the URAA, and as demonstrated by the extensive use of the SEO's Electronic Subsidies Enforcement Library, WTO subsidy notifications also play an important role in the United States' monitoring and enforcement activities under the Subsidies Agreement.

Under Article 25.2 of the Subsidies Agreement, Members are required to report certain information on all measures, practices and activities that, as set forth in Articles 1 and 2 of the Agreement, meet the definition of a subsidy and are specific within the territory of a Member. Last year, 23 subsidy notifications covering the 2004/2005 reporting period were reviewed.[23] The Committee also continued its examination of new and full notifications and updating notifications for earlier time periods. Unfortunately, numerous Members have never made a subsidy notification to the WTO,

[23] The 2005 new and full notifications of the following Members were reviewed in 2006: Armenia; Australia; Brazil; Bulgaria; Canada; China; Cuba; European Communities; Honduras; Hong Kong, China; Iceland; Israel; Japan; Korea; New Zealand; Norway; Qatar; the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu; Singapore; Switzerland; Thailand; Turkey and Uganda.

although many are lesser developed countries.[24] In addition to the standard questions submitted with regard to Member's subsidy notifications, the United States submitted questions pursuant to Article 25.8 of the Subsidies Agreement regarding several subsidy programs administered by Malaysia that appear to be prohibited. While Malaysia responded orally at the fall meeting to some of these questions, it has not yet provided a written response.

2. Review of CVD Legislation, Regulations and Measures

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

To date, 86 Members of the WTO (counting the current 27 Members of the European Union as one) have notified that they have CVD legislation in place, or have notified that they have no such legislation, while 35 Members have not, as yet, made a notification. Among the notifications of CVD laws and regulations reviewed in 2006 were those of China, the former Yugoslavia Republic of Macedonia, Mexico, and Israel.

As for CVD measures, four WTO Members notified CVD actions taken during the latter half of 2005, and four Members notified actions taken in the first half of 2006. Specifically, the Committee reviewed actions taken by Canada, the European Union, Japan, Mexico, and the United States.

3. Article 27.4 Update

Under the Agreement, most developing countries were obligated to eliminate their export subsidies by December 31, 2002. Article 27.4 of the Agreement allows for an extension of this deadline provided consultations were entered into with the Committee by the end of 2001. If the Committee grants an extension, annual consultations with the Committee must be held to determine the necessity of

[24] For further information, see the Report (2006) of the WTO Committee on Subsidies and Countervailing Measures (G/L/798; November 8, 2006).

maintaining the subsidies.[25] If the Committee does not affirmatively sanction a continuation, the export subsidies must be phased out within two years.

To address the concerns of certain small developing countries, a special procedure within the context of Article 27.4 of the Agreement was adopted at the Fourth WTO Ministerial Conference in 2001. Under this procedure, countries whose share of world exports was not more than 0.10 percent and whose Gross National Income was not greater than $20 billion could be granted a limited extension for particular types of export subsidy programs subject to rigorous transparency and standstill provisions. Members meeting all the qualifications for the agreed upon special procedures were eligible for a five-year extension of the transition period, in addition to the two years referred to under Article 27.4.

Antigua and Barbuda, Barbados, Belize, Costa Rica, Dominica, Dominican Republic, El Salvador, Fiji, Grenada, Guatemala, Jamaica, Jordan, Mauritius, Panama, Papua New Guinea, St. Kitts and Nevis, St. Lucia, St. Vincent and Grenadines and Uruguay have made yearly requests under the special procedures adopted at the Fourth Ministerial Conference for small exporter developing countries.[26] These requests were approved by the Committee in 2002, 2003, 2004 and 2005.

In 2006, requests were made by all the countries listed above. All these requests required, *inter alia*, a detailed examination of whether the applicable standstill and transparency requirements had been met. In total, the Committee conducted a detailed review of more than 40 export subsidy programs. At the end of the process, all of the requests under the special procedures were granted. (A chart showing how each of the requests was addressed, as well as the current status of other programs which were not granted extensions, is found in Attachment 4.) Throughout the review and approval process, the United States actively participated and submitted questions on certain Members' export subsidy programs, ensuring close adherence to all of the preconditions necessary for continuation of the extensions, and the faithful implementation of the decisions taken at the Fourth Ministerial Conference.

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

[26] Bolivia, Honduras, Kenya and Sri Lanka are all listed in Annex VII of the Subsidies Agreement and, thus, may continue to provide export subsidies until their "graduation" from Annex VII status (see *Update of Annex VII Calculations* section, which follows). Therefore, these countries have only reserved their rights under the special procedures in the event they graduate during the five-year extension period contemplated by the special procedures. Because these countries are only reserving their rights at this time, the Committee did not need to make any decisions as to whether their particular programs qualify under the special procedures.

In early 2006, some of the Members currently benefiting from the extension under the special procedures have proposed a further 10-year extension until 2018.[27] Under the proposal, only those programs previously granted an extension would be eligible under the same conditions currently in place. Members have exchanged written questions and answers and have engaged in informal consultations regarding the proposal. The Committee's review of the proposal will continue into 2007.

4. Update of Annex VII Calculations

Annex VII of the Agreement identifies certain lesser developed countries that are eligible for particular special and differential treatment. Specifically, the export subsidies of these countries are not prohibited and, therefore, are not actionable as prohibited subsidies under the dispute settlement process. The countries identified in Annex VII include those WTO Members designated by the United Nations as "least developed countries" (Annex VII(a)) as well as countries that had, at the time of the negotiation of the Agreement, a per capita GNP under $1,000 per annum and were specifically listed in Annex VII(b).[28] A country automatically "graduates" from Annex VII(b) status when its per capita GNP rises above the $1,000 threshold. When a Member crosses this threshold it becomes subject to the subsidy disciplines applicable to other developing country Members.

Since the adoption of the Agreement in 1995, the *de facto* interpretation by the Committee of the $1,000 threshold was that it reflected current (*i.e.*, nominal or inflated) dollars. The concern with this interpretation, however, was that a Member could graduate from Annex VII on the basis of inflation alone, rather than on the basis of real economic growth.

In 2001, the Chairman of the Committee, in conjunction with the WTO Secretariat, developed an alternative approach to calculate the $1,000 threshold in constant 1990 dollars. At the Fourth Ministerial Conference, decisions were made

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[27]Antigua and Barbuda, Belize, Barbados, Dominica, Dominican Republic, El Salvador, Fiji, Grenada, Jamaica, Mauritius, Papua New Guinea, St. Kitts and Nevis, St. Lucia and St. Vincent and the Grenadines made the first request as a group. See, G/SCM/W/535. Subsequently, Guatemala, Panama, Costa Rica, Jordan and Uruguay requested an extension.

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

which led to the adoption of this methodology. The WTO Secretariat updated these calculations in 2006.[29]

5. Permanent Group of Experts

Article 24 of the Agreement directs the Committee to establish a Permanent Group of Experts (PGE), "composed of five independent persons, highly qualified in the fields of subsidies and trade relations." The Agreement articulates three possible roles for the PGE: (I) to provide, at the request of a dispute settlement panel, a binding ruling on whether a particular practice brought before that panel constitutes a prohibited subsidy, within the meaning of Article 3 of the Agreement; (ii) to provide, at the request of the Committee, an advisory opinion on the existence and nature of any subsidy; and (iii) to provide, at the request of a WTO Member, a "confidential" advisory opinion on the nature of any subsidy proposed to be introduced or currently maintained by that Member. To date, the PGE has not yet been called upon to perform any of the aforementioned duties. Article 24 further provides for the Committee to elect the experts to the PGE, with one of the five experts being replaced every year.

In the beginning of 2006, the members of the Permanent Group of Experts were: Professor Okan Aktan (Turkey); Mr. Yuji Iwasawa (Japan); and Mr. Asger Petersen (Denmark). Mr. Hyung-Jin Kim's (Korea) term expired in the spring of 2005 and Mr. Terence P. Stewart's (United States) term expired in 2006. The Committee has been unable to reach a consensus as to their replacements.

6. Areas of Focus in 2007

In 2007, the United States will continue to devote special attention to the subsidy notifications submitted to and considered by the Committee. The United States will particularly focus on China's subsidy notification and the Transitional Review Mechanism to ensure that China meets its obligations under its Protocol of Accession and the Agreement. As noted above, in 2007 the Committee will be considering the additional export subsidy extension request by certain small exporter developing countries. Finally, the United States is prepared to take a leadership role in addressing any technical questions or developing country issues that the Subsidies Committee may be asked to consider in the context of issues that may arise within the Rules Negotiating Group.

[29] See, G/SCM/110/Add.3 , May 9, 2006 and G/SCM/110/Add.3/Corr.1, November 14, 2006.

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

1. Accessions

Countries and separate customs territories seeking to join the WTO must negotiate the terms of their accession with current Members

In a typical accession negotiation, the applicant submits an application to the WTO General Council, which establishes a Working Party to review information on the applicant's trade regime and to oversee the negotiations. Accession negotiations involve a detailed review of the applicant's entire trade regime by the Working Party and bilateral negotiations for import market access.

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

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

In 2006, intensive negotiations continued, in particular, with Russia, and Vietnam. As of January 2007, 29 countries have established working parties in the WTO.[30]

a. Russia

In 2006, the United States continued to work with the Russian Federation to complete its accession to membership in the WTO. On November 19, 2006, the United

[30] Accession applicants with working parties established are Afghanistan, Algeria, Andorra, Azerbaijan, Bahamas, Belarus, Bhutan, Bosnia and Herzegovina, Cape Verde, Ethiopia, Iran, Iraq, Kazakhstan, Laos, Lebanon, Libya, Montenegro, Russia, Samoa, Sao Tome and Principe, Serbia, Seychelles, Sudan, Tajikistan, Tonga, Ukraine, Uzbekistan, Vanuatu and Yemen.

States and Russia signed a bilateral market access agreement. The next step in Russia's accession process is completion of multilateral negotiations on a Working Party Report and Protocol of Accession that details the changes Russia will make to bring its trade regime into conformity with WTO rules.

The last formal meeting of the Working Party took place in March 2006. Informal meetings are continuing. Subsidies remain a significant topic of concern for the United States. In particular, the United States is increasingly concerned with the growing role of state-owned and state-trading enterprises in Russia, as well as the Russian government's promotion of strategic industries and will closely monitor these issues as the accession negotiations continue.

Russia's natural gas pricing policies have also been of concern to the United States and several other Members. In particular, the potentially distortive effect that low-priced gas in the domestic market could have on Russian industrial production and internationally-traded energy-intensive products has been an important issue because of the possible resulting adverse impact on U.S. industries. The United States will continue to track the Russian government's policies in this regard and pursue the issue in the multilateral negotiations, as needed.

b. Vietnam

Vietnam's Working Party was established on December 17, 1993. Throughout the accession, the United States worked very closely with Vietnam on its subsidies notification to ensure that Vietnam's subsidy programs would be consistent with its obligations under the Subsidies Agreement upon accession. The United States and Vietnam concluded bilateral market access accession negotiations on May 31, 2006.

Under the terms of the bilateral agreement, Vietnam agreed to eliminate its prohibited subsidies. This will affect all industries, effective immediately upon accession, including the textile and garment industries. The only exception is for two programs, where benefits to current recipients will be phased out over a five-year period.[31]

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[31] In response to concerns raised by the domestic industry over Vietnam's possible provision of prohibited subsidies to its textile and apparel industry despite its accession commitments to terminate such programs, the bilateral agreement contains a unique enforcement mechanism that would allow for the reimposition of quotas on textiles and apparel goods if Vietnam fails to fulfill its obligations to eliminate the subsidies as agreed. In addition, Commerce established a monitoring program for imports of textile and apparel products from Vietnam. Monitoring began with Vietnam's accession to the WTO on January 11, 2007. Initially, Commerce will focus on imports of five sensitive product groups – trousers, shirts, underwear, sweaters and swimwear. Product coverage may change during the life of the monitoring program. Products may be added or removed from monitoring, as appropriate, in response to input from interested stakeholders, changes in trade, or as Commerce's knowledge

On November 7, 2006, the WTO General Council approved Vietnam's membership. Vietnam's National Assembly ratified Vietnam's WTO accession commitments on November 28, 2006, and Vietnam became the 150th Member on January 11, 2007.

2. WTO Trade Policy Reviews

The WTO's Trade Policy Review Mechanism provides USTR and Commerce with another opportunity to review the subsidy practices of WTO Members. These reviews were agreed to as part of the Uruguay Round Agreements with the aim of (1) increasing transparency and promoting understanding of other countries' trade policies and practices; (2) improving the quality of public and intergovernmental debate on important issues; and (3) enabling a multilateral assessment of the effects of trade policy on the world trading system. These "peer reviews" encourage WTO Members to follow WTO rules and disciplines more closely and to fulfill their multilateral commitments.

Trade Policy Reviews (TPRs) focus on the trade policies and practices of a particular country while also taking into account overall economic and developmental needs, policies and objectives, as well as the external economic environment that a country faces. The four largest traders in the WTO (the European Union, the United States, Japan and China) are examined once every two years. The next 16 largest countries, based on their share of world trade, are reviewed every four years. The remaining countries are reviewed every six years, with the possibility of a longer interim period for the least-developed countries. For each review, two documents are prepared: a policy statement by the government under review, and a detailed report written independently by the WTO Secretariat.

These reviews play an important role in ensuring that WTO Members meet transparency requirements concerning their subsidy practices. TPRs also provide a broader context than the Subsidies Committee notification reviews in which to assess a Member's subsidy policies and their role in that Member's economy. In reviewing these reports, USTR and Commerce focus on the information concerning the subsidy practices detailed in the report, but also conduct additional research on potential omissions regarding known subsidy practices that have not been reported. In 2006, USTR and Commerce reviewed 20 Members' TPRs, including those of China, Chinese

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of the domestic industry and the products it produces increases. Every six months, Commerce will conduct a formal evaluation of the information gathered under the monitoring program to determine whether sufficient evidence of injurious dumping exists to warrant self-initiation of an antidumping investigation. The monitoring program will cease on January 19, 2009.

Taipei, Israel and Malaysia.[32] This was the first Trade Policy Review of China since they joined the WTO. USTR and Commerce submitted detailed questions on several areas of China's trade policy, many of which focused on China's subsidies regime. The Secretariat also reviewed the trade policy regime of the United States in March 2006.

CONCLUSION

In 2006, the United States vigorously enforced U.S. rights under the WTO Subsidies Agreement in order to address some of the root causes that give rise to unfair trade distortions, which can cause harm to American workers and industries. In particular, USTR and Commerce continued their work in a number of key areas. These included efforts to seek deeper multilateral subsidies disciplines through the Doha Development Agenda; press China to bring its subsidies practices in line with its international obligations; formulate better disciplines over practices that can distort markets and trade in the steel sector; strengthen ongoing efforts to monitor and challenge subsidies practices that harm U.S. industries and workers; and challenge unfair subsidies to Airbus.

In the Doha Development Agenda subsidy negotiations, the United States has firmly asserted its leadership in support of the need for improved subsidy disciplines, identifying a broad array of subsidy issues that need to be addressed and proposing new disciplines where none currently exist. Identification of enhanced disciplines on trade distorting practices, including subsidies, is particularly important because these practices are the root causes of trade friction. In 2006, the United States continued the technical work of furthering the development of subsidy benefit calculation methodologies that will promote greater predictability in the application of the rules and permit a firmer basis for strengthened disciplines based on quantitative limitations on subsidy benefit amounts. In early 2006, the United States elaborated on its earlier proposal to expand the category of subsidies prohibited under the Subsidies Agreement. This proposal is perhaps the most far-reaching subsidy-related proposals tabled to date in the Rules negotiations. The proposed strengthened disciplines would greatly enhance the United States' ability to address, and potentially deter, subsidy-related unfair trade practices confronting U.S. industries.

In 2006, China submitted its first, long-overdue subsidies notification to the WTO Subsidies Committee. Having conducted extensive research regarding China's industrial subsidy policies, the United States was well-prepared to examine and analyze in depth the notification and pursue numerous issues with respect to the programs notified as well as those not notified. The notification also prompted a series of bilateral

[32] Twenty Members were reviewed in 2006: Hong Kong, China; Colombia; Kenya; Tanzania; Uganda; Kyrgyz Republic; Congo; Bangladesh; Nicaragua; Togo; Chinese Taipei; Iceland; Uruguay; United Arab Emirates; China; United States of America; Djibouti; Angola; Israel; and Malaysia.

meetings in Beijing, including high-level meetings, during which the United States vigorously pressed China to bring its subsidy practices into compliance with its obligations under the Subsidies Agreement. The United States will continue to seek the withdrawal of China's prohibited subsidies, including the initiation of WTO dispute settlement. The United States will also expand its surveillance of China's government practices in order to better identify and, as appropriate, respond to possible subsidy problems. To achieve this, the United States will devote significant resources to China subsidy issues in 2007. On a broader scale, the United States will continue to examine structural problems and distortions in China's economy and pragmatically address concerns regarding trade- and market-distorting practices in the Structural Issues Working Group.

In 2007, USTR and Commerce will promote the goal of strengthening the international subsidy discipline regime and proactively pursue an agenda to safeguard the interests of U.S. industries and workers facing unfairly subsidized foreign competition.

ATTACHMENT 1

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

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

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

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

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

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

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

***Questions and information can be referred to*:**
Carole Showers tel.: (202) 482-3217
fax : (202) 501-7952
e-mail: Carole.Showers@mail.doc.gov
internet: http://ia.ita.doc.gov/esel/index.html

ATTACHMENT 2

TRADE REMEDY COMPLIANCE STAFF:

PRO-ACTIVELY ADDRESSING UNFAIR TRADE PROBLEMS

THE TRADE REMEDY COMPLIANCE STAFF

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

THE TRCS ROLE AND SERVICE

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

TRCS INITIATIVES UNDER WAY

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

TRCS Activities

Washington, D.C.

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

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

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

Overseas

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

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

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

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

Need further information?
Please contact:

Trade Remedy Compliance Staff
Tel: 202-482-3415/Fax: 202-482-6190/email: trcs@ita.doc.gov

ATTACHMENT 3

THE SUBSIDIES ENFORCEMENT LIBRARY

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

First Screen

ELECTRONIC SUBSIDIES ENFORCEMENT LIBRARY

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

WTO Subsidies Notifications

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

Annual Reports to Congress on Subsidies Enforcement

- **Reports from 1998-2006**

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

Description of Choices

WTO Agreement on Subsidies and Countervailing Measures

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

Overview of the Subsidies Enforcement Office

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

Subsidy Programs Investigated by DOC

This links the visitor to information regarding subsidy programs which have been analyzed by Import Administration staff during countervailing duty (CVD) proceedings since 1980. The information is provided by country and then subdivided into various categories, based on the DOC's finding in the proceeding. More detailed information about a program in a specific

case can be easily found by clicking on the hyperlinked cite to the Federal Register notice, in which a complete description of the program and Commerce's analysis is provided. As of December 2006, the number of countries which have had programs investigated in U.S. CVD proceedings was 52.

WTO Subsidies Notifications

This will link the visitor to all unrestricted WTO subsidy notifications, listed either by date or by country. Beside each country's name is a description of the document, the document number and document symbol as well as the date the document was submitted to the WTO. Clicking on the name of a country will lead the visitor to that country's subsidy notification. The notification will provide a list of notified subsidies, in addition to specific information concerning each subsidy program, such as the type of incentive provided, the duration and purpose of the program, and the governing law or provision of the incentive. Although the Subsidies Agreement stipulates that the notification of a subsidy practice does not prejudge its legal status under the Agreement, these notifications do provide detailed information concerning a number of countries' subsidy measures. In the event that less than full information about the program is provided, the Subsidies Enforcement Office, working with other Agencies, seeks more detailed information.

Annual Reports to Congress on Subsidies Enforcement

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

Review and Operation of the WTO Subsidies Agreement - June 1999

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

ATTACHMENT 4

Extension of the Transition Period Pursuant to Article 27.4 of the Agreement on Subsidies and Countervailing Measures		
WTO MEMBER	**NAME OF PROGRAM**	**SUBSIDIES COMMITTEE ACTION*** **
ANTIGUA & BARBUDA*	Fiscal Incentives Act**	Fourth one-year extension granted
	Free Trade/Processing Zones**	Fourth one-year extension granted.
BARBADOS*	Fiscal Incentive Program**	Fourth one-year extension granted.
	Export Allowance**	Fourth one-year extension granted.
	Research & Development Allowance**	Fourth one-year extension granted.
	International Business Incentives**	Fourth one-year extension granted.
	Societies with Restricted Liability**	Fourth one-year extension granted.
	Export Re-discount Facility	**No extension requested.**
	Export Credit Insurance Scheme	**No extension requested.**
	Export Finance Guarantee Scheme	**No extension requested.**
	Export Grant & Incentive Scheme	**No extension requested.**
BELIZE*	Fiscal Incentives Program**	Fourth one-year extension granted.
	Export Processing Zone Act**	Fourth one-year extension granted.
	Commercial Free Zone Act**	Fourth one-year extension granted.
	Conditional Duty Exemption Facility**	Fourth one-year extension granted
BOLIVIA (Annex VII Country)	Free Zone	Reservation of rights. No action taken.
	Temporary Admission Regime for Inward Processing	Reservation of rights. No action taken.
COSTA RICA*	Duty Free Zone Regime**	Fourth one-year extension granted.
	Inward Processing Regime**	Fourth one-year extension granted.
COLOMBIA	**Free Zone Regime**	**No extension requested.**
	Special Import-Export System for Capital Goods & Spare Parts (SIEX)	**No extension requested.**
	Transport Compensation Mechanism	**No extension requested.**
DOMINICA*	Fiscal Incentives Program**	Fourth one-year extension granted.
DOMINICAN REPUBLIC*	Law No. 8-90, to "Promote the Establishment of Free Trade Zones**	Fourth one-year extension granted.
EL SALVADOR*	Export Processing Zones & Marketing Act**	Fourth one-year extension granted.
	Export Reactivation Law	**No extension requested.**
FIJI*	Short-Terms Export Profit Deduction	Fourth one-year extension granted.
	Export Processing Factories/Zones Scheme	Fourth one-year extension granted.
	The Income Tax Act (Film Making & Audio Visual Incentive Amendment Degree 2000)	Fourth one-year extension granted.
GRENADA*	Fiscal Incentives Act No. 41 of 1974**	Fourth one-year extension granted.
	Qualified Enterprise Act No. 18 of 1978**	Fourth one-year extension granted.

WTO MEMBER	NAME OF PROGRAM	SUBSIDIES COMMITTEE ACTION***
	Statutory Rules and Orders No. 37 of 1999**	Fourth one-year extension granted.
GUATEMALA*	Special Customs Regimes**	Fourth one-year extension granted.
	Free Zones**	Fourth one-year extension granted.
	Industrial and Free Trade Zones (ZOLIC)**	Fourth one-year extension granted.
HONDURAS (ANNEX VII COUNTRY)	Free Trade Zone of Puerto Cortes (ZOLI)	Reservation of rights. No action taken.
	Export Processing Zones (ZIP)	Reservation of rights. No action taken.
	Temporary Import Regime (RIT)	Reservation of rights. No action taken.
JAMAICA*	Export Industry Encouragement Act**	Fourth one-year extension granted.
	Jamaica Export Free Zone Act**	Fourth one-year extension granted.
	Foreign Sales Corporation Act**	Fourth one-year extension granted.
	Industrial Incentives (Factory Construction) Act**	Fourth one-year extension granted.
JORDAN*	Income Tax Law No. 57 of 1985, as amended*	Fourth one-year extension granted.
KENYA (ANNEX VII COUNTRY)	Export Processing Zones	Reservation of rights. No action taken.
	Export Promotion Program Customs & Excise Regulation	Reservation of rights. No action taken.
	Manufacture Under Bond	Reservation of rights. No action taken.
MAURITIUS*	Export Enterprise Scheme**	Fourth one-year extension granted.
	Pioneer Status Enterprise Scheme**	Fourth one-year extension granted.
	Export Promotion**	Fourth one-year extension granted.
	Freeport Scheme**	Fourth one-year extension granted.
PANAMA*	Export Processing Zones**	Fourth one-year extension granted.
	Official Industry Register**	Fourth one-year extension granted.
	Tax Credit Certificates (CAT)	**No extension requested.**
PAPUA NEW GUINEA*	Section 45 of the Income Tax Act**	Fourth one-year extension granted.
SRI LANKA (ANNEX VII COUNTRY)	Income Tax Concessions	Reservation of rights. No action taken.
	Tax Holidays & Profits Generated	Reservation of rights. No action taken.
	Concessionary Tax on Dividends	Reservation of rights. No action taken.
	Indirect Tax Concessions - Internal Tax Exemptions	Reservation of rights. No action taken.
	Export Development Investment Support Scheme	Reservation of rights. No action taken.
	Import Duty Exemption	Reservation of rights. No action taken.
	Exemption from Exchange Control	Reservation of rights. No action taken.
ST. KITTS & NEVIS*	Fiscal Incentives Act**	Fourth one-year extension granted.
ST. LUCIA*	Fiscal Incentives Act**	Fourth one-year extension granted.

WTO MEMBER	NAME OF PROGRAM	SUBSIDIES COMMITTEE ACTION***
	Micro & Small Scale Business Enterprise Act**	Fourth one-year extension granted.
	Free Zone Act**	Fourth one-year extension granted.
ST. VINCENT AND THE GRENADINES*	Fiscal Incentives Act**	Fourth one-year extension granted.
THAILAND	**Investment Promotion Incentives**	**No extension requested.**
	Industrial Estate Authority of Thailand	**No extension requested.**
	Export Market Diversification Program	**No extension requested.**
URUGUAY*	Automotive Industry Export Promotion Regime**	Fourth one-year extension granted.

* Countries which have requested an additional ten year extension until 2018.

** Program qualifies under special procedures adopted at the Fourth Ministerial Conference.

*** All programs for which an extension was requested are permitted a two-year phase-out period after the extension period sanctioned by the Subsidies Committee. If no extension period was approved, Members must phase-out the program in two years.

Programs in bold are programs for which no further extension has been requested. Therefore, these programs are subject to the two-year phase-out period. The following programs were granted extensions in 2002, however no extension was requested during the 2003 review: Barbados' Export Re-discount Facility, Export Credit Insurance Scheme, Export Finance Guarantee Scheme and Export Grant & Incentive Scheme; Colombia's Transport Compensation Mechanism; Panama's Tax Credit Certificates (CAT) program; and Thailand's Investment Promotion Incentives, Industrial Estate Authority of Thailand and Export Market Diversification Programs. The following programs were granted extensions in 2003, however no extension was requested during the 2004 review: Colombia's Free Zone Regime and Special Import-Export System for Capital Goods & Spare Parts (SIEX) program; and El Salvador's Export Reactivation Law.