COMMENTS OF CORUS GROUP PLC ON THE INTERNATIONAL TRADE ADMINISTRATION'S NOTICE OF PROPOSED MODIFICATION OF AGENCY PRACTICE CONCERNING THE APPLICATION OF THE COUNTERVAILING DUTY LAW TO PRIVATIZED COMPANIES

These comments are submitted on behalf of Corus Group plc ("Corus") in response to the notice published on March 21, 2003, by the International Trade Administration ("ITA") (68 Fed. Reg. 13897) concerning a proposed modification of ITA's privatization methodology in countervailing duty cases.

Overview - Need for a Simpler Rule

Corus commends ITA for developing a proposal that represents a substantial step forward towards rational coherence and economic realism in the application of the countervailing duty law to privatized companies that, before privatization, had received nonrecurring subsidies. However, certain aspects of the proposal are misguided, apparently owing to a failure to appreciate the implications flowing from basic propositions concerning the nature of the continuing benefit of nonrecurring subsidies and the way in which such continuing benefit is ended by the payment of fair market value in a change of ownership transaction. In addition, certain aspects of the ITA proposal are keyed to imprecise criteria that would be difficult to administer and essentially impossible for petitioners, foreign producers and foreign governments to interpret and apply as guidelines for how – and how not – to meet ITA's criteria for a privatization that would eliminate the benefits of past subsidies. These problems, along with other aspects of the proposed methodology and questions posed in ITA's notice, are addressed below.

Why Payment of Market Value Ends Continuing Subsidy Benefit

In proposing its current Countervailing Duty Regulations,[1] ITA articulated specifically its understanding of the nature of a "benefit" conferred by a governmental financial contribution:

> [A] benefit is conferred when a firm pays less for its "inputs" than it otherwise would pay in the absence of the government-provided input or earns more than it otherwise would earn.[2]

Elaborating further, ITA said:

> In this regard, when we talk about a firm paying less for its inputs than it otherwise would pay (or receiving more revenues than it otherwise would earn), we are referring to the lower price it pays to acquire the thing provided by the government, i.e., money, a good or a service.[3]

Thus, in the context of a nonrecurring subsidy, a company has a continuing benefit (before a market value privatization) in the sense that some portion of the inputs with which it operates were acquired at a lower price than it would have paid absent the government financial contribution. Put another way, the company is enjoying the use of inputs that it acquired at less than their market value.

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[1] Countervailing Duties; Notice of Proposed Rulemaking and Request for Public Comment, 62 Fed. Reg. 8818 (Feb. 26, 1997).

[2] Id. at 8819.

[3] Id. at 8820. This distinction between the fact that a company has a certain input and the fact that it acquired that input at an artificially reduced cost is similar to the distinction drawn by the WTO Appellate Body between the "utility value" and the "market value". United States-Countervailing Measures Concerning Certain Products from the European Communities, WT/DS212/AB/R (December 9, 2002) (hereinafter "AB Decision"), at ¶¶ 102-103.

Once this concept is understood, it is readily apparent why the operation of an asset (e.g., a factory) or a business unit (a division or subsidiary) purchased from the subsidized company at fair market value enjoys no subsidy benefit. Unlike the subsidized company, the producer/new owner of the asset or business unit paid market value for everything it acquired. Thus, it does not operate with any input for which it paid less than it would have paid absent a governmental financial contribution.

It is equally clear that the same reasoning applies to the sale of an entire company for market value. Whereas before that sale the company operated with some inputs acquired at less than market value, that is no longer true after the entire company – including any such input for which the old owners had paid an artificially low price – is bought for fair market value.

This means that anything bought for market value from a subsidized company – whether an asset or a business unit or the entire company – is operated without any subsidy benefit after such a change of ownership for payment of market value.[4]

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[4] The Commentary on the Proposed Regulations noted that ITA "have not closed our minds" to the possibility of some other form of benefit. Id. at 8820. In the long course of the privatization debate, certain petitioner counsel have suggested that a different benefit, one which would endure after market value payment, may exist where the effect of a subsidy is to create productive capacity that, absent the subsidy, would have been uneconomic to create. While Corus does not, as a matter of logic, object to this concept, three important points must be made. First, any privatization decision flowing from the "creation subsidies" concept would have to be based on an ITA determination that the specific effect of a particular subsidy was to create capacity that, absent the subsidy, would never have existed. Second, subsidies provided to preserve existing capacity that has become uneconomic would not fit this logic. Finally, any such "creation subsidies" concept would have to fit the reasoning of the WTO Appellate Body in the decision that gave rise to the present proposed rulemaking.

The proposed new methodology explicitly recognizes that payment of market value is the fundamental test, although it unnecessarily mixes the concepts of "arm's-length transactions," "sale of the entire company" and retention of a "controlling interest" with the correct "fair market value" criterion:

> [A]n interested party may rebut this baseline presumption [of continuing subsidy benefit] by demonstrating that, during the allocation period, a privatization occurred in which the government sold its ownership of all or substantially all of a company or its assets, retaining no controlling interest in the company or its assets, and the sale was an arm's length transaction for fair market value.[5]

This formulation is overly complicated and should be amended in three ways:

First, the methodology should not be limited to a sale of an entire company. The elimination of subsidy benefit by payment of market value occurs whenever all or substantially all of the subsidized company's ownership interest in any part of the company is purchased. Thus a purchaser for fair market value of:

- a plant, a production line or any other asset or group of assets owned by the subsidized firm, or
- a business unit – subsidiary or division – of the subsidized firm, or
- the entire subsidized company, whether in a share sale or an asset sale,

[5] Notice of Proposed Modification of Agency Practice Under Section 123 of the Uruguay Round Agreements Act and Request for Public Comment (hereinafter "ITA Proposal"), 68 Fed. Reg. 13897, 13899 (Mar. 21, 2003).

does not benefit from pre-transaction subsidies in the operation of whatever it is that was purchased. In each case, the purchaser has no inputs acquired at a cost artificially reduced by a government financial contribution.

Second, the retention by the government of a "controlling interest" is not a determinative factor. Where a government sells "all or substantially all" of its interest in a company (or some part thereof) for market value, subsidy benefit is eliminated even if the government retains some method of controlling certain corporate decisions. At most, retention of some control may affect the price paid, and thus whether "market value" was paid.

Finally, "arm's length transaction" is not in and of itself a criterion for determining that continuing subsidization has been eliminated. Rather, the existence of an arm's-length transaction is strong evidence of – and should create a presumption of – the payment of market value. However, as discussed below, there are certain circumstances in which market value payment might not be found in an arm's-length sale. Moreover, there are evidentiary bases on which ITA may determine that market value was paid even where the transaction was not an arm's length sale.

In summary, the proper rule and methodology should be much simpler than that proposed by ITA. Assuming that ITA wishes to maintain its presumption that nonrecurring subsidies confer benefits that continue over a future allocation period, the change of ownership rule should be:

> However, no subsidy benefit accrues to the operation by a new owner of assets, business units or the entire company, provided that the new owner has purchased all or substantially all of the

> ownership interest in such assets, business units or company and has paid the fair market value of what was purchased.

As discussed below, this simpler rule should be applied both in the context of government-to-private sales and in the context of private-to-private sales. Moreover, a determination that the transaction itself was a fair market value sale and encompassed all or substantially all of the seller's ownership interest should end the inquiry; broader issues of the government's influence in overall market conditions (apart from a determination that the sale takes place in a market economy) are not proper subjects of analysis.

With the foregoing in mind, we turn to analyses of specific questions raised by the Request for Public Comment:

Presumption of Continuing Benefit of Nonrecurring Subsidies

For purposes of these comments, Corus will not contest ITA's "baseline presumption" that "non-recurring subsidies can benefit the recipient of a subsidy over a period of time (i.e., allocation period) normally corresponding to the average useful life of the recipient's assets." However, ITA should recall that in numerous past submissions we have pointed out that this "baseline presumption" is predicated on entirely arbitrary propositions which distort, rather than assist, ITA's analysis of the nature and effects of capital infusions by governments. ITA's failure to base its analysis on economically rational principles makes this and many other aspects of subsidy determinations an entirely haruspical exercise.

What Is Fair Market Value and How Should ITA Determine That Fair Market Value Was Paid?

Corus agrees in substance with ITA's formulation of the meaning of "fair market value":

> The basic question before us in analyzing fair market value is whether the government, in its capacity as seller, sought and received, in the form of monetary or equivalent compensation, the full amount that the company or its assets were actually worth under existing market conditions.[6]

The following, alone or in combination, may provide sufficient evidence that fair value was in fact paid:

Arm's-Length Transaction

Corus does not take issue with ITA's (and the SAA's) definition of an "arms-length transaction":

> [a] transaction negotiated between unrelated parties, each acting in its own interest, or between related parties such that the term of the transaction are those that would exist if the transaction had been negotiated between unrelated parties.[7]

In a transaction between two private parties, a determination that the transaction met this definition of arm's-length sale should end the inquiry. In the private-to-private context, an arm's-length transaction is necessarily one in which fair market value is paid. Accordingly, the purchaser receives no benefit from past subsidies.[8]

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[6] ITA Proposal, at 13900. A more precise formulation would focus on the purchaser, not the seller: "… whether the purchaser paid to the seller government, in the form of …." The ITA formulation smacks of "cost to the government' instead of "benefit to the recipient."

[7] Id.

[8] See AB Decision, at ¶ 124.

As to privatization (and government-to-private sales in general), some further inquiry may or may not be appropriate. Both the Appellate Body[9] and Judge Restani's initial decision in Delverde I observe that a government seller may have non-commercial objectives or may impose requirements that detract from the market value nature of the transaction. Accordingly, ITA should presume that market value is paid in an arm's-length sales in which a government was the seller, but may entertain rebuttal of that presumption in the form of evidence that the government bargained for elements other than the highest price, imposed non-commercial considerations on the sale, limited the number of bidders, gave a preference to a certain bidder or class of bidders, etc. In assessing such rebuttal evidence, however, ITA should keep several considerations in mind:

First, rebuttal evidence is probative only when it shows that governmental action led to a price lower than market value. In some cases, a government may seek to promote the sale by offering inducements to purchasers that increase the transaction price above market value. Such actions may in some circumstances constitute new subsidies to the purchaser, but they cannot be deemed evidence that the sale was for less than market value. Obviously, payment of a price greater than market value eliminates the benefit of past subsidies just as would payment of market value.

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[9] Id.

Second, the presumption of subsidy benefit elimination can be rebutted only when the rebuttal evidence shows that the transaction price was reduced materially[10] below fair market value. Governmental actions not shown to have a material negative impact on the price are not relevant.

Finally, ITA should be aware that the mere fact that a government seller does not accept the highest price bid does not, in and of itself, warrant the conclusion that fair market value was not paid. The high bidder may not have responded properly to the invitation for bids. Or the high bidder might be a company of limited financial resources, raising doubt that it could make the payments required by its bid. For these and other reasons, ITA in such a case must inquire as to why the highest bid was rejected.

Other Evidence

ITA should consider all evidence bearing on the question whether the transaction price reflects at least the fair market value of what was purchased. Such evidence would include:

- Independent analyses or appraisals of the value of what was sold[11]
- In the case of assets, the original cost less depreciation

[10] The use of words that have no established definition – "materially," "significantly," etc. – will pose problems unless ITA establishes some definition that will enable respondents, petitioners and those crafting transactions to quantify what ITA means.

[11] Such analyses made contemporaneous with or in preparation for the sale are obviously probative. However, a well-done subsequent study by a reputable independent entity may also be probative.

- Contemporaneous similar sales

- In a share sale, the movement of the share price in the open market immediately after the public offering.[12]

These examples are illustrative only. In some cases not involving an arm's-length transaction, these types of evidence may provide the best approach to analyzing the market value issue. They are also of particular relevance in government-seller transactions, where it may be hotly disputed whether the transaction was at arm's length in the commercial sense.

Corus notes that ITA also expresses an intention to consider various factors in assessing the "fair market value" issue.[13] However, we have concerns that factors (1) and (4) on page 13900 of the Federal Register notice may represent imprecise thinking.

Whether the government created artificial barriers to bidding on a privatization may be a factor of some relevance, but its effect on the bidding process and in particular on the level of the bids would be extremely difficult to analyze. Unless there is a clear way of quantifying the effect of such governmental barriers on the bid prices – at least to the point of determining whether the effect is "material" – Corus respectfully urges that this factor not be considered.

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[12] Analysis of this factor, of course, should factor out market movements to isolate movements specifically related to the value of the company. This is regularly done by economists in securities fraud lawsuits.

[13] ITA Proposal, at 13900.

The factors listed in number 4 are clearly relevant. Again, however, Corus cautions that the issue is whether such factors had a material impact on reducing the transaction price below fair market value.

"Broader Conditions"

The ITA Proposal takes the position, as we understand it, that a transaction might be found to have been made at fair market value, but that ITA might find "that the broader market was severely distorted by government action."[14] Such distortion would apparently not have to be quantified by the party alleging it, nor by the Department.[15] This concept has no place in ITA's privatization analysis.

Before addressing the general concept of "broader conditions," it is worth noting that two of the four "conditions" – "related incentives" and "legal requirements" – are in fact specific to the transaction under investigation. These are legitimate issues for ITA to examine in determining whether "fair market value" was paid. Their relevance, of course, depends on a sufficient quantification of their effect on transaction price to permit a determination whether that effect (if any) was "material."

Items denominated 1 and 4 are in fact "broader conditions" that one would consider only for the purpose of assessing whether the market itself was seriously distorted. Assuming that these factors do not rise to the level of a determination that the transaction took place in a non-

[14] Id.

[15] Id., at n.8.

market economy, Corus urges in the strongest possible terms that ITA not engage in "market distortion" analysis, for the following reasons:

First, whatever concerns may arise concerning these conditions and the market as a whole, they do not go to the relative position of a purchaser who bought assets, business units or a company from a subsidized seller as compared with a purchaser who bought the same thing in that country from an unsubsidized seller. Whatever may be the overall market distortions, a purchaser who bought a steel mill from a subsidized seller for its "fair market value" would pay the same price as a purchaser who bought the same steel mill at "fair market value" from an unsubsidized seller. That being the case, there can be no basis for determining that the purchaser from the subsidized seller enjoys a subsidy benefit.

Second, any analysis of such "broader conditions" at the time of the sale would have to compare such "broader conditions" to those existing at the time(s) the subsidies were bestowed. If the "market distortion" existed when the subsidies were provided, there can be no ground to argue that a later sale should be disregarded simply because the market conditions remained distorted. Put another way, whatever artificial benefit the subsidies conferred at the time of the bestowal was a benefit whose nature, amount and duration reflected the {distorted} market condition existing at the that time. Surely the analysis of the later transaction under the same market conditions is not inappropriate.

Third, this form of analysis will merely be speculative, imprecise and – for both ITA and the parties – expensive and inconclusive.

Finally, this sort of analysis would tend to reject the effect of privatization in less-developed countries where legal systems and market structures are less fully developed. Yet it is those very countries that are the particular focus of U.S. policy encouraging privatization of government-owned industries.

With specific reference to item 4 – the effect on the market of subsidization of other companies – both ITA and the Appellate Body have made it clear that it is not the purpose of the countervailing duty law to remove the general market distortion of subsidies, but rather to offset the benefits to the specific recipient.[16]

In summary, Corus submits that consideration of "broader conditions" not directly related to the transaction at issue has no place in ITA's analysis. A decision based on such factors would inevitably fail WTO scrutiny.

Presumptions vs. Safe Harbors

Corus is greatly concerned that the series of rebuttable presumptions contemplated by the ITA proposal are unworkable and impose undue burdens on the parties. Moreover, the burdens are not placed equally on petitioners and respondents. The core issue – whether the change of ownership is done at fair market value – appears in ITA's proposal to be one as to which respondents have the burden of "demonstrating" all the complex elements.[17] But then, as to the "broader conditions" that may persuade ITA to ignore a market value transaction, the level of

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[16] AB Decision, at ¶ 42, citing Certain Steel Products from Austria, 58 Fed. Reg. 37217, 37264 (July 9, 1993) (General Issues Appendix).

"demonstration" required of petitioners is much less, and it explicitly does not extend to any quantification.[18]

If ITA must presume that nonrecurring subsidies provide continuing benefits over an allocation period, that presumption should cease when evidence of a change in ownership is presented. At that point,

> an investigating authority undertaking an administrative review has an obligation under Article 21-2 of the SCM Agreement to determine whether a "benefit" continues to exist when information suggesting that a benefit exists is presented to that authority.[19]

Under this mandate, ITA makes a determination in the way it makes other determinations – without burdens on one party or the other to rebut a presumption. As to an issue as complex as a market value price determination, this approach is not only mandated by the Appellate Body, it is the fair and equitable approach.

Corus submits, however, that it is appropriate for ITA to consider publishing "safe harbors" or guidelines with respect to when a privatization (as opposed to private-to-private transactions) will be deemed to eliminate the continuing benefit of past nonrecurring subsidies. This would be desirable not only to simplify proceedings before ITA, but also to advance the

[17] ITA Proposal, at 13899-13900.

[18] Id. and n. 8.

[19] AB Decision, at ¶ 141.

U.S. policy of encouraging privatization, especially in developing countries. Corus would suggest that the following "safe harbors" are appropriate.[20]

- In a share transaction, sale of X% of the company's (or subsidiary's) sales will be deemed a sale of "all or substantial all" of the company (or subsidiary).

- Where shares are sold in a public offering, fair market value will be deemed to have been paid where the offering is to the general public without material restrictions and either

  - the per-share price was at least as high as that determined by an independent evaluation conducted by a reputable entity experienced in making such evaluations, or

  - the price of the shares in after-offering trading on an exchange or other open, active market (e.g., NASDAQ) did not rise materially above the public offering price in a way that is atypical from other public offerings.

- The sale of a government-owned company (or a plant or business unit of such company) through a competitive bidding process will be deemed a sale not priced below market value if

  - the bidding process is open to enough bidders to ensure a competitive process, and

  - the terms of the bid solicitation either do not contain restrictive conditions not found in private-to-private transactions (e.g., employment, investment or export guarantees), or any such restrictions are not sufficient to reduce the value of what is sold materially below fair market value.

In addition, it would be appropriate for ITA to establish a similar, but far simpler, safe harbor for private-to-private sales:

- the sale of all or substantially all of a privately-owned subsidized company (or all or substantially all of a plant or business unit of such company) to a private purchaser (or purchasers) in an arm's-length transaction in a reasonably

[20] This list is not meant to be exhaustive.

> competitive market will be deemed a sale for market value that extinguishes any continuing benefit of past subsidies to that company, plant or business unit.

Specific ITA Questions

- Continuing Benefit Amount
- Partial or Gradual Sales
- Holding or Parent Companies
- Concurrent Subsidies

Corus has not had experience with any of these fact patterns and will thus leave comment on these questions to other parties. We may address these issues in our rebuttal comments.

- Effective Control

As the previous discussion has made clear, it is payment of market value, not whether the seller retains some control despite having sold all or substantially all of its ownership interest, that creates a situation in which operations of what is purchased (a plant, a business unit or the entire company) operates after the transaction with no continuing benefit from past subsidies. To the extent retention by the government of some degree of control has any relevance, it is relevant only to the extent it might affect (reduce) the value of the company. Thus a market value price could be lower for such a company than would have been the case if the government had retained no control.

ITA's Notice makes specific mention of "golden shares," a subject on which Corus can speak with authority. ITA will recall that, in privatizing British Steel, the U.K. Government retained a golden share which gave it, for a limited period, the right to be consulted on certain corporate structure issues. It gave the government no control over the operations of the

company. Accordingly, the retention of the golden share was not found by ITA to be any barrier to a determination that British Steel had been privatized for fair market value.

CONCLUSION

The ITA Proposal constitutes a significant step in the right direction, but it must be modified in certain respects as set forth herein. Corus' recommendations can be grouped in four principal categories:

1. The methodology should focus clearly on the payment of market value as the reason that operation of the purchased plant, business unit or company does not benefit from past nonrecurring subsidies.

2. In a government-to-private sale, conditions imposed on the sale by the government are relevant only to the extent that they reduce the sale price materially below fair market value. Thus quantification of the price effect of such government limitations is essential.

3. Government actions or policies not directly related to the sale, the effects of which are on broader market conditions, should not be relevant to ITA's privatization analysis. Moreover, examination of such matters would add greatly to the cost of the proceeding and would produce only speculation, not hard data.

4. Instead of the presumptions currently contemplated, ITA should develop safe harbors that will both simplify these investigations and permit foreign companies and governments to structure privatizations and other ownership change transactions in ways that will meet ITA's criteria.