中 华 人 民 共 和 国 商 务 部

MINISTRY OF COMMERCE OF THE PEOPLE'S REPUBLIC OF CHINA
2, DONG CHANG'AN STREET, BEIJING, CHINA 100731

December 10, 2007

PUBLIC DOCUMENT

The Honorable David Spooner
Assistant Secretary for Import Administration
U.S. Department of Commerce
Attention: Import Administration
Central Records Unit, Room 1870
14th Street and Constitution Avenue, N.W.
Washington, D.C. 20230

Attn: Lawrence Norton and Anthony Hill

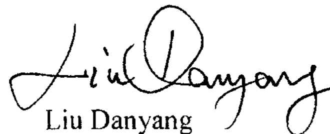
Re: BOFT's 2nd MOE Comments

Dear Mr. Secretary:

With this submission the Bureau of Fair Trade for Imports and Exports of the Ministry of Commerce of the People's Republic of China ("BOFT") provides its response to the Commerce Department's Federal Register Notice, dated October 25, 2007, seeking *additional* comments on the adoption of an MOE (market-oriented enterprise) under which the Department would grant an individual respondent in China market-economy treatment for the purposes of calculating antidumping margins.

BOFT's additional comments are set forth in the attached document.

Respectfully submitted,



Liu Danyang
Deputy Director General
Bureau of Fair Trade, Ministry of Commerce
People's Republic of China

Before the United States Department of Commerce
International Trade Administration

Bureau of Fair Trade for Imports and Exports of the Ministry of Commerce of the People's Republic of China

Response to the Commerce Department's *Second* Request for Comments Concerning Market Economy Treatment for Individual Respondents in Antidumping Proceedings Involving China

Dated: December 10, 2007

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INTRODUCTION

With this submission, the Bureau of Fair Trade for Imports and Exports of the Ministry of Commerce of the People's Republic of China ("BOFT") provides its response to the Commerce Department's Federal Register Notice, dated October 25, 2007, seeking *additional* comments on the adoption of an MOE (market-oriented enterprise) under which the Department would grant an individual respondent in China market-economy treatment for the purposes of calculating antidumping margins.

This submission has four sections:

Section A reiterates BOFT's position that the Commerce Department's factual findings about China's economy that are cited to justify application of the CVD law to China also require the Commerce Department to terminate its designation of China as a non-market economy for AD cases, or, at a minimum, reverse the presumption that all Chinese exporters are controlled by the Chinese Government.

Section B argues that, given the initiation of 7 combined CVD and AD cases in the past year, fundamental fairness requires the Commerce Department to adopt and implement an MOE test immediately.

Section C explains that the current statute, the Commerce Department's existing regulations, and the Department's long-standing practices provide complete legal authority for the Commerce Department to adopt an MOE test under which individual Chinese respondents could obtain market-economy treatment in an AD case.

Section D provides practical suggestions on how the questions that the Commerce Department can identify an MOE operating within a broader NME environment.

And *Section E* explains why the Department need not adopt a special approach for those inputs that are, arguably, inextricably linked to the broader operating economic environment, such as land, labor and capital.

A. The Decision To Impose CVD Duties Against China Requires The Commerce Department To Re-Evaluate Whether To Treat China As A Non-Market Economy In Antidumping Cases, Or, At a Minimum, Reverse the Presumption For Those Exporters Not Investigated

The Commerce Department's decision memoranda justifying its recent decision to apply the CVD law to China set forth numerous *factual findings* that the *Commerce Department itself* has made concerning the Chinese economy of today. These findings can be summarized by the following three factual statements:

> "China's economy {of today} presents a significantly different picture than the traditional communist economic system of the early 1980's, i.e. the so-called "Soviet style economies"[1]
>
> "{P}rivate industry now dominates many sectors of the Chinese economy, and entrepreneurship is flourishing. . . .The role of central planners is vastly smaller."[2]
>
> "The PRC Government has eliminated price controls on most products; market forces now determine prices of more than 90 percent of products traded in China." [3]

BOFT submits, once again[4], that such factual findings raise serious questions about the legality and propriety of the Commerce Department's continued designation of China as an NME. Very simply, given that the Commerce Department itself has admitted that (1) the Chinese economy of today is vastly different from the "Soviet-style" non-market economy that existed when the NME AD methodology was designed, and (2) there is a sufficient market economy "to determine whether the PRC Government has bestowed a {countervailable} benefit upon a Chinese

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1 Commerce Department Memorandum dated March 29, 2007 Re: Whether the Analytical Elements of the *Georgetown Steel* Opinion Are Applicable To China's Present-Day Economy, prepared for Inv. No. C-570-907, *Coated Free Sheet Paper from China*, (hereinafter "*Georgetown Steel* Memorandum") at 4.

2 *Id.* at 10.

3 *Id.* at 5.

4 *See e.g.* Case Brief of Government of China, submitted in CFS Paper Investigation

producer," it makes no logical or economic sense for the Commerce Department to continue to designate China as an NME.

Over more than 20 years of accelerating reforms in its economic system, China has established a *bona fide* market economy system. Such a market economy system is expressly written into the Chinese constitution. And indeed, by many accounts China has a more developed market economy system than some of the countries that the U.S. has recently designated as market economies.

It is for this reason that, in recent years, many other WTO Members have adjusted their designations of China's economic system to conform to present-day reality. Currently, many countries, including ASEAN member states, Australia, New Zealand, South Africa, Brazil, Argentina, Egypt and South Korea have formally granted China market economy status under their antidumping laws. Modifications made by these countries to their domestic antidumping rules show their active recognition of the achievements of China's reforms and market opening initiatives.

Finally, we note that the issue of China's market economy status in antidumping investigations also involves the WTO principle of fair and non-discriminatory treatment in trade. It relates to whether China's exporting industries and related enterprises can compete as equals with the exporters of other countries, which are recognized by the United States as market economies, in a fair, equitable and non-discriminatory environment. China has followed the U.S. legal and procedural requirements and submitted applications to the United States for market economy status and market-oriented industry status in a number of cases on a number of occasions. However, the United States has persistently refused China's application on various pretexts and fully ignored the evidence and facts that have been provided by China. Because the

United States has persisted in designating China as a non-market economy country in its antidumping investigations, Chinese enterprises are not getting fair and non-discriminatory treatment in antidumping investigations.

BOFT therefore believes that the Department has sufficient justification to terminate its designation of China as a non-market economy and appropriately recognize China as a market economy country under U.S. antidumping law.

Even if the Department continues to treat China as an NME, the Department's factual findings underlying the Department's decision to apply the CVD law to China require Commerce, at a minimum, to reverse the current presumption that Chinese exporters are controlled by the state. The presumption should now be that Chinese exporters are not controlled by the state, but rather are market-oriented.

Very simply, the Department's current presumption is completely at odds with *more recent* factual findings that the Commerce Department itself has made about China's "present-day" (2006-2007) economy. These recent Commerce Department factual findings demonstrate unequivocally that the *factual assumption* underlying the Department's presumption that markets do not exist in China because of Chinese government control is simply no longer true. China is no longer a nation in which "bubbles of capitalism" exist.[5] And, more importantly, if there are any distortions within Chinese economy created "state control," they are now deemed identifiable and measurable.

Indeed, BOFT submits that the application of CVD law to China itself requires reversal of the presumption. The application of CVD law to China completely undermines the basis for the presumption to apply the NME methodology to all Chinese respondents. Any meaningful

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5 *Chrome-Plated Lug Nuts from the People's Republic of China:Final Determination of Sales at Less Than Fair Value*, 56 Fed. Reg. 46,153 (Sept. 10, 1991)

consideration of NME versus market-economy treatment must be informed by the fact that U.S. domestic industries now possess the ability to seek relief through CVD cases for state-created distortions.

The original rationale underlying the Department's decision in the 1980s that CVD law was inapplicable to NMEs centered around two tenets fundamental to the definition of what a subsidy is under the WTO Agreement on Subsidies and Countervailing Measures: subsidies must be specific and provide a financial benefit.[6] The Department believed that it was impossible in NMEs to determine that a subsidy was specific: the "Soviet-style economies {prevalent in NMEs} at that time made it impossible to apply these criteria because they were so integrated as to constitute, in essence, one large entity."[7] The Department also observed in the 1980s an even more fundamental characteristic of subsidization as it applied to the market:

> "We believe a subsidy (or bounty or grant) is definitely any action that distorts or subverts the market process and results in a misallocation of resources. . . . In NMEs resources are not allocated by a market. With varying degrees of control, allocation is achieved by central planning. Without a market, it is obviously meaningless to look for misallocation of resources caused by subsidies. There is no market process to distort or subvert.... It is this fundamental distinction—that in an NME system the government does not interfere in the market process but supplants it—that has led us to conclude that subsidies have no meaning outside the context of a market economy."[8]

The existence of a subsidy is unquestionably linked to the existence of the market it distorts – subsidies cannot affect distorting behavior from firms if there is no market to distort. The determination that allows the CVD law's application to China necessarily means, by extension, that government interference does not supplant the market, a fact the Department implicitly accepts in its NME Status Memo in *Lined Paper*.[9]

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6 WTO Agreement on Subsidies and Countervailing Measures, art. 1, 2

7 *Georgetown Steel* Memorandum at page 10.

8 *Carbon Steel Wire Rod from Czechoslovakia: Final Negative Countervailing Duty Determination*, 49 Fed. Reg. 19,370 (May 7, 1984)

9 NME Status Memo at 51.

To put it in the context of a specific case, in both the CFS paper CVD case and the circular-welded pipe cases, the Department concluded that the *sales values* of the Chinese exporters were perfectly acceptable for use in the calculation of CVD rates.[10] Given that the sales values the Department utilized in the CVD case are simply the sum of the *net prices of individual (home market and export) sales* by the Chinese CFS exporter, there is no reason why these same sales prices could not be used in the AD proceeding.

Quite simply, markets exist in China. Thus, if "'market forces now determine the prices of more than 90 percent of products traded in China,'" as the Department recently declared, then the prices of less than 10 percent of products in China are not set by market forces.[11] Yet, even with this small percentage of non-market oriented products, their prices apparently still provide meaningful measures of value; if the prices did not do so, then the Department would not be able to apply CVD law to China since subsidies, as defined by the WTO Agreement on Subsidies and Countervailing Measures, must create a specific benefit that is *measurable.*[12] Therefore, if Chinese prices meaningfully measure value such that they permit the Department to measure benefits within the context of a CVD case,[13] then it follows that these very same prices must also be reliable enough to use in the calculation of normal value in an AD case.

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[10] *See Coated Free Sheet Paper from People's Republic of China: Amended Preliminary Affirmative Countervailing Duty Determination*, 72 Fed. Reg. 17,484 (April 9, 2007) (hereinafter "*CFS Paper CVD Preliminary Determination*"). *See also* Memorandum to File, dated March 29, 2007, Re: Calculations for the Preliminary Determination for Gold East Paper, Prepared for Inv. C-570-907, *Coated Free Sheet Paper from China*. *See also* Calculation Package for Commerce Department's Preliminary Determination in Circular Welded Pipe from China.

[11] The Department went to great lengths to use the noun "market forces" as opposed to the noun "market" in both the NME Status and *Georgetown Steel* Memoranda. However, this is a silly distinction: if market forces exist, so does the market.

[12] WTO SCM Agreement, art. 14, 19 (it must be possible to calculate the benefit)

[13] *See CFS Paper CVD Preliminary Determination* at the "Grant Programs," "Income Tax Program," "VAT and Duty Exemptions," and "Domestic VAT Refunds for Companies Located in the Hainan Economic Development Zone" sections of the FR where the Department measured benefit using internal values derived in China.

Whether the economic logic is accepted or not, **consistency in treatment of the evidence requires the approach we propose**. The Commerce Department must apply consistent standards in CVD and AD proceedings when analyzing the exact same evidence. Application of consistent evidentiary standards requires use of home market and third country sales prices, rather than surrogate values, to determine normal value for the AD calculation.

It cannot be otherwise. We are not aware of any legal or logical basis under which the Department could declare that values are reliable in the CVD framework but unreliable in the AD framework.

B. Fundamental Fairness and Due Process Require That the Commerce Department Adopt an MOE Test Immediately

Fundamental fairness and due process require that the Department adopt a realistic, achievable MOE test immediately, so that entities who find themselves subject to petitions based on inconsistent AD and CVD methodologies will have some redress for this unfair treatment. The Department has been aware of the inconsistency between the assumptions underlying its NME AD methodology and the factual premise of its CVD methodology for some time, and its continued delay in crafting rules to address the situation is unacceptable.

A basic underpinning of administrative law is that "those regulated by an administrative agency are entitled to 'know the rules by which the game will be played.'"[14] However, notwithstanding that **seven** combined AD/CVD cases have been filed against China, the Department has still not proposed rules addressing the admitted tension between applying a market-economy oriented CVD law to China and continuing to designate China as a non-market

14 *Alaska Professional Hunters Association v FAA*, 177 F.3d 1030, 1035 (1999) quoting Holmes, Holdsworth's English Law, 25 Law Quarterly Rev. 414 (1909)).

economy for antidumping cases. BOFT reminds the Department that the Department itself stated that "the features and characteristics of China's present-day economy also suggest that modification of the Department's current NME methodology may be warranted," and that adopting an MOE mechanism was one such "modification."[15] BOFT asks that the Department honor its promise and develop, as expeditiously as possible, a mechanism to allow Chinese exporters to seek MOE status in AD cases.

C. Solid Legal Authority Exists for the Department to Grant MOE Status to Chinese Exporters

The Department's Federal Register Notice seeking a second round of comments specifically requested an answer to the following question: "Whether there is a legal basis for a MOE." The answer to the question is a resounding "yes." Solid legal authority exists for the Department to develop and apply an MOE test.

1. The statute provides legal authority.

It is important to remember that the statute does *not require* that Commerce apply a special AD calculation methodology to NME countries. Rather, the applicable statutory provision states:

> **(c) Nonmarket economy countries**
>
> (1) In general
>
> If—
>
> (A) the subject merchandise is exported from a nonmarket economy country, and
>
> (B) the administering authority finds that available information does not permit the normal value of the subject merchandise to be determined under subsection (a) {home market or third country sales},

15 *Georgetown Steel Memorandum* at 11.

> the administering authority shall determine the normal value of the subject merchandise on the basis of the value of the factors of production utilized in producing the merchandise ....[16]

The above **statutory language** makes clear that the key factor in deciding whether to apply the special NME AD methodology in a particular case is not simply that the case targets imports from a country that the Commerce Department has determined is an NME country, but rather whether "**available information**" permits normal value to be determined from home market or third country sales prices.

Consequently, if the Commerce Department were to make a *factual finding* that sufficient "available information" can be obtained from the Chinese exporters to calculate AD margins using home market or third country prices, then the Commerce Department would have the full legal authority to use the Chinese exporter's home market or third country prices when calculating the AD margin.

2. <u>The Commerce Department regulations provide legal authority.</u>

Similarly, the **Department's regulations** state that in AD cases against NME countries the Department "normally" will calculate AD margins according to the special factors of production methodology.[17] By utilizing the word "normally" instead of simply "shall," the Department's regulations explicitly recognize that there may well be exceptions to the rule; that is, there may well be cases against an NME country in which it is not necessary to utilize the factor of production methodology to calculate normal value.

The distinction between a statutory mandate and a regulatory preference is critically important, one which the Department acknowledged when it established the market-oriented

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[16] 19 U.S.C. 1677b(c).

[17] *See* 19 C.F.R. 351.408.

industry ("MOI") test under which respondents could presumably receive market-economy treatment and thus also face potential CVD cases:

> "{That Congress amended the U.S. antidumping laws in 1988 to allow the Department to calculate AD margins using the market economy methodology reflects} recognition of attempts by the traditional NME countries to evolve toward market-oriented economies... Congress clearly contemplated a situation in which a sector of an NME may be sufficiently free of NME distortion so that the actual prices and/or costs incurred in the NME could be used in the dumping calculations and render meaningful results."[18]

While this interpretation only discussed the possibility of one sector, the Department clearly established that the market economy methodology could be applicable to NME respondents.

3. **The Department's MOI practice provides legal authority.**

The Department itself has stated that it has legal authority to apply market economy methodology to NME respondent under certain circumstances. The Department's Final Rule on Antidumping Duties and Countervailing Duties in 1997 contains the following unambiguous statement:

> "Section 773(c)(1) of the [Tariff] Act permits (underline added) the Department, in certain circumstances, to use the 'market economy' methodology set forth in section 773(a) to determine normal value in an NME case."[19]

To identify those situations where it can apply the market economy methodology, the Department developed a so-called "market oriented industry" or "MOI" test.

Although the Department chose not to codify the MOI test in the regulation, it did so not out of lack of legal authority, but rather because it perceived a deficiency in the MOI test in "identifying situations where it would be appropriate to use domestic prices or costs in a NME as the basis for normal value..."[20] Such conclusion can be confirmed by the numerous cases after

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18 *Final Negative Countervailing Duty Determination: Oscillating Ceiling Fans from the People's Republic of China*, 57 Fed. Reg. 24018 (June 5, 1992).

19 Department of Commerce International Trade Administration 19 CFR Parts 351,353, and 355 Antidumping Duties; Countervailing Duties, Final Rule, 62 Fed. Reg. 27296, 27364 (May 19, 1997).

20 62 Fed. Reg. at 27364.

1997 where the Department received and analyzed whether a particular respondent industry qualified as an MOI under the test. Needless to say, the Department would not have undertaken this exercise in all these cases if it believed that it could not apply market-economy AD rules to Chinese exporters.

4. The Department's long-standing practice of utilizing a Chinese exporter's actual cost data of its market-economy import purchases of major inputs also provides legal authority.

The Department already has a long standing practice of utilizing, in certain situations, actual cost data from Chinese exporters. Specifically, in certain situations the Commerce Department will utilize a Chinese exporter's actual cost of purchasing imported material inputs in the AD margin calculation. Indeed, when it revised its "market-economy input prices" rule in 2006, the Department stated:

> The Department is now instituting a rebuttable presumption that **market economy input prices are the best available information** for valuing an entire input when the total volume of the input purchased from all market economy sources during the period of investigation or review exceeds 33 percent of the total volume of the input purchased from all sources during the period.

The market economy inputs rule in both its earlier form and revised form confirmed that the Department has legal authority to use a NME producer's actual purchase price in calculating normal value. Under this rule, when certain pre-defined standards are met, an NME producer's actual purchase price for an input can be used to value normal value. That methodology is closer to the market economy constructed value methodology stipulated under section 773(e) than to the NME normal value methodology.

The market economy's inputs rule is also consistent with the statutory mandate to use the best available information to calculate accurate dumping margins. In fact, the Department itself went as far as stating the following:

> In general, the purpose of the antidumping statute is to "determine margins as accurately as possible." Rhone Poulenc, Ind. v. United States, 899 F.2d 1185, 1190 (Fed. Cir. 1991). ... **Requiring the use of surrogate value in a situation where actual market-based prices incurred by a particular firm are available would be contrary to the statutory purpose**. Where we can determine that an NME producer's input prices are market determined, accuracy, fairness, and predictability are enhanced by using those prices. Therefore, using surrogate values when market-based values are available would, in fact, be contrary to the intent of the law.[21]

The courts have resoundingly approved the Department's valuation of an input based on the respondent's actual import purchases from a market economy supplier. Indeed, the Federal Circuit has explicitly endorsed the rule that, where "input prices are market determined, accuracy, fairness and predictability are enhanced by using those prices. Therefore, **using surrogate values when market-based values are available would, in fact, be contrary to the intent of the law.**[22]"

The above stated court decisions and the Department's practice demonstrates that the Department has clear legal authority to forsake NME dumping calculation methodology and adopt a market economy equivalent constructed value methodology when market-based prices are available.

D. The MOE Test Should Consist of Application of a Rebuttable Presumption

It is BOFT's position, as detailed above, that no factual or legal justification exists for continuing to apply a presumption that all Chinese exporters are controlled by the Chinese Government. Or stated differently, it is BOFT's position that the Commerce Department should

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[21] *Lasko Metal Prod., Inc. v. United States*, 43 F.3d 1442, 1446 (quoting Oscillating Fans and Ceiling Fans from the People's Republic of China, 56 Fed. Reg. 55271, 55275 (Dep't Commerce Oct. 25, 1991) (final determination of sales at less than fair value)) [hereinafter *Fans from the PRC*].

[22] *Lasko*, 43 F.3d at 1446 (quoting *Fans from the PRC*, 56 Fed. Reg. 55275).

adopt a reputable presumption that market-economy AD rules will be applied to all Chinese exporters unless Petitioners present concrete rebutting this presumption for a particular exporter.

In practice, reversal of the current NME presumption, as it concerns calculation of normal value, means that mandatory respondents would receive an AD questionnaire that is largely the same as the market economy questionnaire.[23] This is consistent with the language of the statute, which says that the NME methodology should be applied only if "the administering authority finds that available information does not permit the normal value of the subject merchandise to be determined under subsection (a) {home market or third country sales}".[24] **This cannot be determined unless the DOC actually collects the "available information" on which normal value would normally be based.** Now that the basis for the NME presumption has been extinguished by the Department's recent factual findings about the Chinese economy, this information should at least be collected before making a decision that alternative information is needed.

As with the separate rate test, the Department would apply the same approach irrespective of a respondent's ownership. That is, *all companies* – whether private or state owned – *would be presumed market oriented.* State ownership would not result in the automatic denial of market oriented treatment to state owned companies. After all, if state owned companies are not automatically denied separate rate status because the state owns them, it cannot be assumed that state ownership also distorts their home market prices, third country prices, and production costs.

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23 Because we fully agreed with them, our comments on this point are similar to the comments provided by the China Chamber for Imports and Exports for Chemicals, Metals and Minerals during the Department's first round of MOE comments.

24 19 U.S.C. 1677b(c).

Indeed, this is a position the Department has effectively already adopted. In the CFS Paper case, the Department ruled that firms with state ownership can operate separately and independently in the Chinese market, such that government subsidies exert influence leading the firm to behave in a market-distorting manner. Specifically, before it decided to withdraw from the CVD investigation, Department had decided to apply the CVD law to the state-owned Shandong Chenming Paper Holdings Ltd. ("Chenming").[25] If this state-owned company was not sufficiently separate and independent from the Government of China, the Department could not have applied the CVD law to it, since, as the Department recognized in the original *Georgetown Steel* case, doing so would lead to the illogical and ultimately meaningless conclusion that the state specifically granted a financial benefit to itself.[26] If Chenming was not an independently run company capable of reacting to market forces, then Chenming would be a part of the NME entity and assigning the company an individually calculated margin, whether in the CVD or AD context, would be a futile exercise.

There are also multiple examples of the Department examining state owned companies in AD and CVD cases against market economy countries, in which state ownership itself did not deny the respondent equal treatment with its privately owned competitors.[27] There is no reason to treat state-owned companies in countries denominated as NMEs any differently.

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[25] See *Coated Free Sheet Paper* at 17489 ("The Shouguang State-Owned Asset Administration owned 31.24 percent of Chenming during the POI. Therefore, for purposes of the creditworthiness determination, we are preliminarily treating Chenming as government-owned...")

[26] This is further supported by China's WTO Accession agreement which specifically provides that state-owned enterprises can receive "specific" subsidies simply by being the "predominant" recipient of a subsidy. Clearly, in negotiating China's accession agreement, other WTO members contemplated the notion of whether state-owned enterprises could be separate from the Government of China such that CVD law could apply. *See* WTO Protocol on the Accession of the People's Republic of China, Article 10.

[27] For example, consider the Department's treatment of Brazilian state-owned steel producer CSN relative to its privatized competitor Usiminas in the context of simultaneous AD and CVD investigations on hot-rolled steel. *See Final Affirmative Countervailing Duty Determinations: Certain*

Like the separate rate test, the questions asked in the Section A questionnaire for purposes of determining MOE status should focus on whether the company legally possesses the ability to operate independently of the government (i.e., the de jure requirement) and thus respond to market forces and whether the company actually does (i.e., the de facto requirement). This test is perhaps the most important question in defining MOEs: Since we know the market exists, the question becomes whether a potential respondent is free from government interference such that it can operate in the market.

Private enterprises, whether owned by domestic or foreign parties, can indubitably respond in the affirmative; they are by definition free from government control. The Government of China, both in law and practice, guarantees the ability of private and foreign-owned enterprises to operate freely, notwithstanding regulations typical of market economy countries. Therefore, MOE status for such companies would simply rest on the firm's ability to demonstrate that the company is privately owned and operates without government interference in much the same manner as the Department's current separate rate test.

The question then becomes whether enterprises that are partially or completely owned by the state are sufficiently separate and independent from the state such MOE status could apply. While private ownership alone should be sufficient to establish a company's separation and

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Steel Products From Brazil, Part IV, 58 Fed. Reg. 37295 (July 9, 1993) and *Final Determinations of Sales at Less Than Fair Value: Certain Hot-Rolled Carbon Steel Flat Products, Certain Cold-Rolled Carbon Steel Flat Products, Certain Corrosion-Resistant Carbon Steel Flat Products, and Certain Cut-to-Length Carbon Steel Plate From Brazil*, Part IV, 58 Fed. Reg. 37091 (July 9, 1993). As a general matter, in a market economy context the Department has uniformly applied its AD and CVD rules whether the respondent is state-owned or privately-held. *See generally Final Affirmative Countervailing Duty Determination: Certain Steel Products From Austria*, Part IV, 58 Fed. Reg. 37217 (July 9, 1993) (addressing various general issues from numerous market economy CVD investigations involving both state-owned and privately-held respondents) and *Notice of Final Determinations of Sales at Less Than Fair Value: Certain Hot-Rolled Carbon Steel Flat Products, Certain Cold-Rolled Carbon Steel Flat Products, Certain Corrosion-Resistant Carbon Steel Flat Products, and Certain Cut-to-Length Carbon Steel Plate From France*, Part IV, 58 Fed. Reg. 37125 (July 9, 1993) (applying standard AD methodology to French state-owned producer Usinor Sacilor and its affiliates).

independence, the existence of state ownership does not deny it. State ownership is not a determinative factor, which the Department is well aware of this, as its precedent is littered with numerous CVD cases in which state-owned companies in market economies were subjected to CVD investigations.[28] Moreover, the presence of state-owned enterprises in numerous market economies, such as in Europe, provides substantial proof that ownership alone is not dispositive proof of state control.[29]

Rather the relevant analysis should focus on whether state-owned companies are actually state-run companies. Again, the Department's experience in applying separate rates provides instructive guidance on this matter as the Department has continually judged state-owned companies to possess sufficient separation.

Beyond these special Section A questions, all fully examined Chinese respondents would be asked to complete the market economy Section B (comparison market sales), Section C (U.S. sales), and Section D (actual costs, not factors of production) questionnaires.

Only if petitioners are able to identify information submitted in response to these questionnaires, or from elsewhere, establishing the existence of distortions in a respondent's prices or costs that could not be addressed through the CVD law would the Department seek

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28 *See, e.g., Final Affirmative Countervailing Duty Determination: Certain Steel Products From Austria*, Part IV, 58 Fed. Reg. 37217 (July 9, 1993) (addressing Austrian-specific issues for state-owned respondents as well as various general issues from numerous market economy countervailing duty investigations involving both state-owned and privately-held respondents); *Final Affirmative Countervailing Duty Determinations: Certain Steel Products From Brazil*, Part IV, 58 Fed. Reg. 37295 (July 9, 1993) (involving Brazilian state-owned producers); and *Final Affirmative Countervailing Duty Determinations: Certain Steel Products From France*, Part IV, 58 Fed. Reg. 37304 (July 9, 1993) (involving French state-owned producers).

29 *See, e.g., Final Affirmative Countervailing Duty Determination: Certain Steel Products From Austria*, Part IV, 58 Fed. Reg. 37217 (July 9, 1993); *Final Affirmative Countervailing Duty Determinations: Certain Steel Products From France*, Part IV, 58 Fed. Reg. 37304 (July 9, 1993); *Final Affirmative Countervailing Duty Determinations: Certain Steel Products from Germany*, Part IV, 58 Fed. Reg. 37315 (July 9, 1993); *Final Affirmative Countervailing Duty Determination: Certain Cut-to-Length Carbon-Quality Steel Plate From Italy*, Part II, 64 Fed. Reg. 73244 (Dec. 29, 1999).

additional information, possibly including factors of production. And, importantly, absent any governing laws or regulations that restrict or control a firm's ability to sell and react to market forces (which the separate rate test already examines for export markets), the Department would never determine that state ownership in itself precludes a firm from receiving market oriented economy treatment. Rather, MOE treatment should be presumed for all mandatory respondents, until petitioners allege and prove otherwise.

E. No Special Treatment Is Warranted For Land, Labor, or Capital

In its request for comment, the Department mentions specific inputs – land, labor, and capital – which it apparently views as especially problematic. We are puzzled by the Department's focus on land, labor and capital because all available evidence demonstrate that neither labor, land nor capital in China are distorted by government intervention.

As for labor, the Department itself has made a factual finding that labor rates are not established by the Government of China, rather they are determined by market forces:

> Wages between employer and employee appear to be negotiated, as opposed to government-set, as evidenced by the variability in wages across regions, sectors, and enterprise demands. Certain rights, such as the right to compensation and choice of employment, are afforded to workers; employers, while hampered in the ability to reduce staff, are generally free to make independent decisions regarding labor.

Given its own factual finding, there is no basis to conclude that labor costs are determined on a non-market basis.

As for land, our primary comment is that, for the most part, land does not play a role in the AD margin calculation. Land is a fixed asset. Under U.S. GAAP principles, for almost all industries,[30] land is not depreciated since it is not consumed (i.e., land is indefinite).[31] If land is

[30] An example of an industry where land would be depreciated or coasted is mining.

not depreciated, then land does not affect costs, and therefore land has no affect on the cost of production. Because it has no effect on the cost of production, land plays no role in the AD margin calculation. Consequently, the alleged distortions cited by the Department (in its August 30th Memorandum) are largely irrelevant for this exercise.

As for capital costs, we submit that there is no basis for the Department's conclusion (set forth in the CFS Paper case) that all lending by state-owned banks is influenced (and therefore distorted) by the Government. We submit that such conclusion cannot reasonably be drawn from the evidence presented in the CFS Paper case.

Indeed, the issue of government control or influence over bank lending was addressed extensively in the Department's own "Private Financial Experts Verification Report." That report summarized the statements of Expert 2 regarding government interference as follows:

> The expert reiterated that China's banking sector has experienced significant reforms in the past five years. . . . However, as part of the international listings, China has achieved a greater centralization of financial, as well as political, decisions. The expert emphasized that the current administration has centralized management of the banks and has achieved this through, *inter alia*, requiring central approval for certain larger loans and standardizing lending criteria. The expert also noted that CBRC staff has been trained by foreign governments to implement onsite measures and to conduct audits and investigations of bank practices.
>
> The expert noted that legal prohibitions against local government influence were not effectively implemented between 1995 and 2003. However, the creation of the CBRC in 2003 was the turning

[31] American Institute of Professional Bookkeepers, *Depreciation Under GAAP (For Book Purposes)*, Mastering Depreciation (Professional Bookkeeping Certification), June 30, 2005, at page 13 and 21. ("Similarly, although land is not depreciated (because it does not wear out), improvements to land, such as paving or fences, are depreciated because these improvements wear out or become obsolete over time…{In discussing how depreciation is reflected on the financial statement} Land is not depreciated, so {the book value} amount does not change from year to year.).

> point, leading to significant decreases in the extent of local government interference in lending decisions.[32]

In addition, the experts interviewed by the Department agreed that "recent trends have moved away from local government influence over bank operations,"[33] "the central government may try to reign in lending, but the reality is that the central government cannot dictate or try to control the flow of lending,"[34] and "the CBRC has been quite active and effective in the past two years."[35]

The statements by the Department's experts were essentially mirrored in the interviews in the "Government of the People's Republic of China Verification Report: Policy Lending." Several factors have contributed to the sharp decline in the influence of local and central governments in lending decisions: (1) the adoption by the banks of modern corporate governance systems; (2) improved risk management which includes more centralized authority for loan approvals and a requirement that no single person have the ability to approve a loan; (3) holding individual bank officials accountable for lending decisions; (4) the creation of the CBRC itself, along with the regulations enforced by the CBRC; (5) CBRC supervision and inspection of bank practices; and (6) the introduction of international strategic investors and its consequent effect on bank governance and practices.[36] As reported by the Department:

> The CBRC explained that it focuses on the procedures that establish bank independence to ensure that local governments do not influence bank activities. With respect to informal, back-door

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32 Private Financial Experts' Verification Report, prepared by the Department for the CFS Paper Case, at 6.

33 Id. at 11.

34 Id. at 15.

35 Id. at 7.

36 Bank Verification Report, prepared by the Department for the CFS Paper case, at 5-9, and 19.

> influence over managers, the CBRC cannot necessarily prevent every individual bank managers from breaking the rules.[37]

Notwithstanding the inability of the CBRC to ensure that its rules are followed in every single instance, the facts show that local government influence in lending decisions is negligible. As indicated by the verification report, "the CBRC has found that very few NPL's have been caused by local government influence since the reforms have been put in place."[38] This statement is at least indirectly confirmed by the annual statements of the policy and commercial banks which all show a sharp decline in non performing loans over the past five years through 2006.[39] As an example, the 2006 annual report of the China Development Bank shows non-performing loans going from 2.42 percent in 2002 to 0.96 percent in 2005 (with a further decline to 0.75 percent in 2006).[40] The only conclusion one can fairly draw from this information is that to the extent that the local or central governments influence banks to make loans on a non-commercial basis, the instances of such influence are tiny relative to the banks overall lending and had declined sharply by 2005. Thus, the record evidence in the CFS Paper case directly contradicts the conclusion that all lending by state-owned banks is "influenced" by the Chinese Government.

In short, for purposes of establishing an MOE test for use in AD case, there is no need for special treatment for land, labor or capital.

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[37] Id. at 7-8.

[38] Id. at 7.

[39] GOC March 15, 2007 submission at Exhibit SQ-19, SQ-20, and SQ-22.

[40] GOC May 29, 2007 submission at Exhibit 13 (2006 Annual Report, at 6).