Affirmative Comments of AG der Dillinger Hüttenwerke and GTS Industries S.A. to Proposed Modification of Privatization Methodology

Pursuant to the request for public comment published in the *Federal Register* on March 21, 2003 (68 Fed. Reg. 13897), we submit the following affirmative comments on behalf of AG der Dillinger Hüttenwerke ("Dillinger") and GTS Industries S.A ("GTS") concerning the Department's proposed modification to its privatization methodology.[1]

I. Introduction

For more than a decade now, the Department's privatization methodology has been under challenge in the U.S. courts and before the WTO Dispute Settlement Body. Each tribunal reviewing the Department's methodology has emphasized that the key analysis should focus upon whether the post-sale company actually benefitted from assistance granted prior to the change in ownership.[2] Unfortunately, rather than altering its methodology to directly analyze benefit to the recipient, the Department has had a history of simply adjusting the presumptions it uses as a surrogate for this required analysis.

The Department's current proposed methodology is no exception. By its own admission, the proposed methodology is structured as a "sequence of rebuttable presumptions," starting with the presumption that previously-bestowed subsidies are fully passed through to a privatized company. None of the Department's proposed presumptions involves a direct analysis of whether a privatized company actually received a benefit from prior financial contributions

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[1] Dillinger and GTS are European producers of steel products against whom the Department has assessed countervailing duties based upon application of its privatization methodology. Dillinger and GTS were respondents in two of the cases examined in WTO Dispute No. DS212. *See* Certain Cut-to-Length Carbon Quality Steel from France, No. C-427-817; Cut-to-Length Carbon Steel Plate from Germany, No. C-428-817.

[2] Delverde, SrL v. United States, 202 F.3d 1360 (Fed. Cir. 2000).

bestowed on the state-owned enterprise. Accordingly, the Department's proposed methodology continues to be at odds with the obligations of the United States under the WTO agreements and therefore cannot be seen as implementing the Appellate Body's report in DS212 involving countervailing measures imposed by the United States on certain products from the European Communities.

II. Discussion

A. Benefit to the Recipient

Two foundational principles of countervailing duty law are that (1) countervailing duties can only be imposed upon a company's products if it is shown that the company is receiving a "benefit" from a "financial contribution" made by a government or public body[3] and (2) countervailing duties may not exceed the amount of subsidy found to exist.[4] These principles were reiterated by the Appellate Body in its report striking down the Department's privatization methodology in *United States - Countervailing Measures Concerning Certain Products from the European Communities* and form the crucial legal underpinning for that decision.[5] Therefore, any methodology imposed by the Department in response to this decision should be narrowly tailored in order to meet these requirements.

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[3] 19 U.S.C. §§ 1677(5)(B) (defining "subsidy"); WTO Agreement on Subsidies and Countervailing Measures, art. 1.1 [hereinafter *SCM Agreement*]; Delverde, 202 F.3d at 1366 (stating that a "subsidy can only be determined by finding that a person received a 'financial contribution' and a 'benefit' by one of the acts enumerated in [19 U.S.C.] §§ 1677(5)(D) and (E)").

[4] *SCM Agreement*, arts. 19.4 & 21.1.

[5] *See United States - Countervailing Measures Concerning Certain Products from the European Communities*, DS212, AB-2002-5 at paras. 78-83 & 139 [hereinafter Appellate Body Report].

Unfortunately, the Department's proposed methodology is simply structured as a "sequence of rebuttable presumptions" that are not narrowly focused upon the issue of whether a recipient company is actually benefitting from a government-provided financial contribution. Nor does the proposed methodology insure that countervailing duties will not be imposed in an amount exceeding the actual amount of subsidy currently benefitting the recipient. Accordingly, it is likely that application of the revised methodology would result in the imposition of countervailing duties in situations in which there has been no precise determination of benefit to the recipient in violation of U.S. law and WTO obligations. This is evident from an analysis of the three presumptions proposed by the Department.

1. Presumption 1 (Continuation of the Benefit of Non-Recurring Subsidies)

In its request for public comment, the Department states that the "baseline presumption" of its proposed methodology is that "non-recurring subsidies can benefit the recipient over a period of time (*i.e*., allocation period) normally corresponding to the average useful life of the recipient's assets."[6] The Department then goes on to limit the evidence that can rebut this baseline presumption to the sole situation of a privatization "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."[7] Such a severe limitation on the evidence that can rebut the Department's baseline presumption clearly violates the foundational principle of benefit to the recipient discussed above. For

[6] Request for Public Comment, 68 Fed. Reg. 13897, 13899 (Mar. 21, 2003).

[7] Id.

example, the Department's methodology would allow it to ignore completely a partial privatization and thereby impose countervailing duties at a level that exceeded the benefit actually received by the recipient.

The Appellate Body has never permitted such a narrow interpretation of the requirements imposed by the *SCM Agreement*. To the contrary, in its report in *Lead and Bismuth*, the Appellate Body affirmed the Panel's findings that "when an investigation . . . takes place, the investigating authority must establish the existence of a 'financial contribution' and 'benefit' during the relevant period of investigation."[8] In reaching this decision, the Appellate Body reiterated that "[i]n an original investigation, the investigating authority must establish that *all* conditions set out in the *SCM Agreement* for the imposition of countervailing duties are fulfilled."[9] While the Appellate Body did not agree with the Panel's decision that this same requirement also "*always*" applied in administrative reviews, the Appellate Body did find that an investigating authority must address those issues that have been raised before it concerning continuing existence of a "benefit."[10] The Appellate Body in no way limited the issues to be addressed by an investigating authority solely to situations involving a full privatization in which the government maintains no controlling interest in the company or its assets. It must also be noted that, in the past, the Department has consistently applied its privatization methodologies to

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[8] *United States-Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, DS138, AB-2000-1, para. 63. (May 10, 2000) (quoting *United States - Imposition of Countervailing Duties On Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating In the United Kingdom*, DS138, Report of Panel, para. 6.73 (Dec. 23, 1999)).

[9] Id. This passage was quoted with approval by the Appellate Body in this current dispute. *See* Appellate Panel Report, para. 147.

[10] Id.

both partial and full privatizations without distinction.

Accordingly, the Department cannot impose a baseline presumption that the benefit of non-recurring subsidies continues for the entire average useful life of a company's assets in such a manner that would permit it to (1) impose countervailing duties during an investigation in an amount in excess of the actual benefit received by the recipient in contravention of Article 19 of the *SCM Agreement* or (2) to continue the imposition of countervailing duties in an administrative or sunset review in an amount exceeding the amount necessary to counteract the specific subsidy in contravention of Article 21 of the *SCM Agreement*.

2. Presumption 2 (Privatization at Arm's-Length for Fair Market Value)

In analyzing the impact of a privatization at arm's-length and for fair market value, the Department must again be guided by the principle of benefit to the recipient discussed above. As stated in the Appellate Body Report,

> the word "benefit", as used in Article 1.1(b) [of the *SCM Agreement*], implies some kind of comparison. This must be so, for there can be no "benefit" to the recipient unless the "financial contribution" makes the recipient "better off" than it would otherwise have been, absent that contribution. In our view, *the marketplace provides an appropriate basis for comparison* in determining whether a "benefit" has been "conferred", because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favourable than those available to the recipient in the market.[11]

Accordingly, the entire analysis of benefit must be made from the perspective of the recipient. Did the recipient receive a financial contribution on terms more favorable than those available in the market? In fact, in *Canada-Aircraft* the Appellate Body specifically found that the cost to

[11] Appellate Body Report, para. 98 (quoting *Canada - Measures Affecting the Export of Civilian Aircraft*, AB-1999-2 at para. 157 (Aug. 2, 1999) [hereinafter *Canada-Aircraft*]).

the government granting the financial contribution is not relevant in determining the existence or level of a benefit to the recipient.[12]

Therefore, the Department is incorrect in stating that

> the basic question . . . 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.[13]

The fact that a government may place conditions on a sale (*e.g*., retention of redundant workers, promises of future investments) that private commercial sellers would not normally require, does not mean that the purchasers received a countervailable benefit from such conditions. To the contrary, the retention of redundant workers or the promise of future investment may place an additional financial burden upon the purchaser. As long as the conditions are known prior to sale, they become part of the bargained-for exchange between the parties and are factored into the fair market value of the privatization transaction.

Accordingly, the Department's proposed methodology must be amended in order to require that a privatization transaction be analyzed from the point of view of benefit to the recipient and not cost to the government.

3. Presumption 3 (Broader Market Conditions)

Under the Department's proposed methodology, the effects of an arm's-length, fair market value privatization will be disregarded if domestic producers demonstrate that:

> the market itself was so distorted by the government that there is a reasonable basis for believing that the transaction price was meaningfully different from

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[12] *Canada-Aircraft*, paras. 151-161.

[13] Request for Public Comment, 68 Fed. Reg. at 13900 (emphasis added).

what it would otherwise have been absent the distortive government action.[14]

The Department does not describe the level of evidence necessary to reach its "reasonable basis" standard or define the phrase "meaningfully different." It does however clearly state that "[n]either the parties nor the Department would be required to quantify by how much the actual transaction price differed from an 'undistorted market' value."[15]

Thus, the Department's proposed methodology would allow it to ignore the effects of an arm's-length, fair market privatization and impose countervailing duties against a company's products without ever determining the existence or amount of any countervailable benefit currently being received by the company. This is directly at odds with the principle of benefit to the recipients discussed above. Countervailing duties may only be imposed against a company's production if it is shown that the company received a countervailable benefit, and the amount of countervailable duties cannot exceed the level of benefit determined.[16] Moreover, macroeconomic distortions by their very nature are general, affecting all enterprises within a country, and therefore cannot meet the specificity requirement necessary for the imposition of countervailing duties.[17]

Nothing in the Appellate Body Report can dictate or justify such a radical departure from the principle of benefit to the recipient. The discussion at paras. 120-127 of the report, stating that a privatization at arm's length and for fair market value will not *always automatically* require a

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[14] Id.

[15] Id. at n.8.

[16] *See* discussion *supra* at pp. 2-3.

[17] *SCM Agreement*, art. 2 (defining "specificity").

determination of no benefit, means only that an irrebuttable presumption of no benefit may not be imposed.[18] This discussion was not meant to alter the fundamental requirements of benefit to the recipient or bring into countervailing duty investigations a new inquiry as to macroeconomic conditions. To the contrary, the Appellate Body stated that "privatization at arm's length and for fair market value . . . *presumptively* extinguishes any benefit received from the non-recurring financial contribution bestowed upon a state-owned firm" and that this presumption can only be rebutted if it is established that the "*benefit from the previous financial contribution* does indeed continue beyond privatization."[19] Thus, far from diminishing the requirement of benefit to the recipient, the Appellate Body reiterated that countervailing duties could be imposed on the production of a privatized company only if it was shown that the company had received a benefit from the previous financial contributions paid to the state-owned enterprise.

The Department's proposed foray into the area of macroeconomic analysis also marks a radical departure from all previous administrative practice. The Department has always maintained that market distortions play no role in the assessment of countervailing duties. For example, in its final determination regarding certain steel products from Austria, the Department stated:

> The CVD law is designed to provide remedial relief as a result of subsidies; it is

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[18] Appellate Body Report, paras. 120-27; *see also* id. at para 158 (describing the Panel report as imposing a presumption of no benefit that applied "*necessarily* and *always*" and "*automatically*").

[19] Appellate Body Report, para. 126 (emphasis added); *see also* id. at para 158 (stating that the *SCM Agreement* "permits an investigating authority to evaluate evidence directed at proving that, regardless of privatization at arm's length and for fair market value, the new private owner may nevertheless enjoy *a benefit from a prior financial contribution* bestowed on the state-owned enterprise." (emphasis added)).

> not intended to recreate the *ex ante* conditions that existed prior to the bestowal of such subsidies. Indeed, the remedy provided by law, additional duties, does nothing to eliminate excess capacity caused by the subsidization. Thus, there is no reason to require the recipient of the subsidies to correct the distortion in order to avoid or lift the duties. . . . The fact that the productive capacity may have been created or continues to exist is an irrelevant inquiry and beyond the scope of the law.[20]

In fact, during its oral argument before the Appellate Body, the United States confirmed that "it continues to stand by [this] principle."[21] Moreover, the Appellate Body reiterated that, "for purposes of determining the continued existence of a 'benefit' under the *SCM Agreement*," the relevant value is the "*market value*" based upon the particular privatization transaction and not the "*utility value*" based upon broader economic considerations.[22]

In addition, the specific market and economic conditions listed by the Department in its proposed methodology would have no relevance within the countervailing duty analysis currently required by U.S. law. The absence of market conditions such as unfettered interplay of supply and demand applies only to non-market economy ("NME") countries. Because the U.S. countervailing duty laws do not apply to NME countries, the economic considerations listed by the Department would have no practical relevance in its countervailing duty investigations.[23] Moreover, before the Department revokes a country's NME status, it makes a thorough investigation as to whether the country has put into place all the necessary elements of a market-

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[20] Final Affirmative Countervailing Duty Determination: Certain Steel Products from Austria, 58 Fed. Reg. 37217, 37264 (1993) [hereinafter General Issues Appendix].

[21] Appellate Body Report, para. 101.

[22] Id. at para 102.

[23] *See* Georgetown Steel Corp. v. United States, 801 F.2d 1308 (Fed. Cir. 1986).

based economy.[24] Thus, a decision by the Department to revoke a country's NME status means that the factors listed under the last prong of the proposed privatization methodology do not exist. It must also be remembered that each of the twelve cases involved in the current WTO dispute involve western European countries with highly-developed, long-established market economies. Thus, none of the factors listed under the last prong of the Department's proposed methodology could be used to diminish the effect of the fair market value privatizations at issue in each of those cases.

Accordingly, the Department should abandon any attempt at analyzing broader market or economic conditions and instead focus its inquiries upon specific benefit to the recipient as required by law.

B. Issues Requiring Further Elaboration

In its request for public comments, the Department states that many important details of its proposed methodology "require further elaboration."[25] The Department then lists six specific issues upon which it encourages parties to comment. As with the other elements of the Department's proposed methodology discussed above, the Department must be guided by the principle of benefit to the recipient in resolving the listed issues.

1. Continuing Benefit Amount

As described in the request for public comment, the Department's proposed methodology

[24] *See* 19 U.S.C. 1677(18); *see also* Memorandum *from* Albert Hsu, Barbara Mayer, and Christopher Smith through Jeffrey May, Director, Office of Policy, *to* Faryar Shirzad, Assistant Secretary, Import Administration: Inquiry into the Status of the Russian Federation as a Non-Market Economy Country under the U.S. Antidumping Law (June 6, 2002).

[25] Request for Public Comment, 68 Fed. Reg. at 13901.

consists of a sequence of all-or-nothing presumptions, which would subject a foreign producer to full pass-through of previously bestowed subsidies if not fully satisfied. For example, in discussing the evidence required for rebutting the "baseline presumption" that the benefit of a non-recurring subsidy continues for the entire average useful life of a recipient's assets, the Department states that:

> [i]f we determine that the government has not transferred, as a result of the sale, ownership and effective control over all or substantially all of the company or its assets, *then our analysis of the transaction will stop and the baseline presumption of a continuing benefit will not be rebutted*.[26]

As discussed above, however, the mere fact that a government retains some control in a privatized company cannot automatically justify the imposition of countervailing duties based upon the full amount of subsidies bestowed on the state-owned enterprise prior to privatization. Instead, the Department must make a careful analysis of the benefit actually received by the privatized company, and the amount of countervailing duties imposed may not exceed the amount of benefit determined.[27]

In measuring the amount of benefit to the recipient, the Department must follow the standards set out by the Appellate Body in *Canada-Aircraft*. Thus, the Department may only find a countervailable benefit if and to the extent that the recipient received a financial contribution on terms more favorable than those available to the recipient in the market. The cost to the government is not relevant in determining the existence or level of benefit to the recipient.[28]

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[26] Id. at 13900 (emphasis added).

[27] *See* discussion *supra* pp. 3-4.

[28] *See* discussion *supra* pp. 5-6.

2. Concurrent Subsidies

The treatment of subsidies given to encourage or otherwise concurrent with a privatization should similarly be analyzed using the principle of benefit to the recipient. As long as the assistance, such as debt forgiveness, is negotiated by the parties as part of the privatization transaction, any value of the assistance will be reflected in the purchase price paid by the new owners. There would therefore be no countervailable benefit accruing to the newly privatized company from the assistance.

3. Private Sales

The principle of benefit to the recipient applies with equal force to private-to-private transactions. As determined by the U.S. Court of Appeals for the Federal Circuit in *Delverde*, private-to-private sales can extinguish pre-sale subsidy benefits.[29]

4. Partial or Gradual Sales

As discussed above with respect to *Continuing Benefit Amount*, even partial privatizations can require the Department to analyze whether the full amount of previously bestowed subsidies continue to benefit the post-sale company. It is only in carefully analyzing and quantifying the continuing benefit to the recipient that the Department can fulfill its obligations under Articles 19 and 21 of the *SCM Agreement*.

5. Effective Control

As discussed above with respect to *Continuing Benefit Amount*, the fact that the government maintains partial control over a privatized company does not automatically expose the company

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[29] Delverde, 202 F.3d at 1368 (discussing the effect of a private-to-private change in ownership).

to countervailing duty liability based upon the full amount of pre-privatization assistance. Rather, the Department must carefully analyze and quantify the actual countervailable benefit still accruing to the privatized company.

6. Holding or Parent Companies

The Department's current practice of automatically allocating assistance received by a parent or holding company to all of its production subsidiaries violates the principle of benefit to the recipient. Instead of an automatic allocation of subsidies, the Department must carefully analyze the facts of each transaction and determine whether a particular subsidiary is benefitting from assistance received at the parent company level. This is especially true in situations in which a production company having no prior history of subsidization is merged into a corporate group that had received previous assistance.

C. Consultations with the European Communities

Given the long history of this dispute between the United States and the European Communities, it would be most efficacious for the United States to conduct serious consultations with the European Communities in an attempt to devise a privatization methodology satisfactory to both parties. This would save considerable resources of the WTO and the member countries involved in this dispute and significantly strengthen the WTO and its dispute settlement process.

III. Conclusion

The Department should abandon its reliance upon presumptions of continuing benefit and instead base its revised methodology upon a direct and thorough analysis of whether a privatized company actually benefits from prior financial contributions bestowed on the state-owned enterprise. Only in this way can the Department properly implement the Appellate Body's

report in DS212.

Given the fact that the Department's methodology has now been under challenge for over a decade, it is incumbent upon the United States to fully and finally comply with its WTO obligations. To do otherwise weakens the WTO and its dispute settlement process. The United States should be at the forefront of the WTO compliance, and the continuing need for other countries to resort to the dispute settlement process in order to force U.S. compliance merely wastes precious administrative resources and breeds contempt for the WTO within the general public.