

**SUBSIDIES ENFORCEMENT
ANNUAL REPORT TO THE CONGRESS**

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

FEBRUARY 2002

Executive Summary

Vigorous enforcement of the rules and disciplines of the World Trade Organization (WTO) Agreement on Subsidies and Countervailing Measures (Subsidies Agreement) continues to be a top priority for the Office of the U.S. Trade Representative (USTR) and the Department of Commerce (Commerce). The Subsidies Agreement is the primary instrument for reining in the use of distortive subsidy practices worldwide. The United States pursues enforcement of its rights under the Subsidies Agreement through its participation in the WTO Subsidies and Countervailing Measures Committee, bilateral contacts, multilateral pressure and, where justified, WTO dispute settlement proceedings. The basic goal of these activities is to deter distortive subsidization and prevent or remedy harm caused to U.S. producers and workers as a result of such subsidies. By working actively to address some of the most important causes of unfair trade distortions, the subsidies enforcement program is helping to strengthen the open, competitive trading environment that is of enormous benefit to American producers and consumers alike.

In the coming year, the Administration will continue to take strong, pro-active steps to address the impact of distortive subsidies on American firms and their workers in both the United States and foreign markets. To accomplish this, the Administration will assertively put forward its affirmative agenda in the forthcoming WTO rules negotiations, in order to effectuate our objective of strengthening the international subsidy discipline regime. The existing WTO disciplines on subsidies, while substantial, prohibit only a narrow range of subsidy practices. Permitted subsidies can also distort markets, and therefore, need to be addressed. In this regard, the mandate agreed to at the WTO's Fourth Ministerial Conference is critically important because it provides an avenue to deal with these other practices and to inform the discussions of subsidy and antidumping measures in a constructive manner. Equally important, the negotiating mandate will permit the United States to include in its affirmative agenda proposals that will defend the legitimate interests of U.S. exporters, who are increasingly becoming subject to unfair trade cases abroad.

The negotiating mandate agreed to at the Fourth Ministerial Conference also included the initiation of negotiations aimed at eliminating harmful fish subsidies. The United States has believed for some time that the depleted state of the world's fisheries is a major economic and environmental concern, and that subsidies contribute to overcapacity and have substantial trade-distorting effects. At Doha,

the United States fought for the inclusion of negotiations to discipline these subsidies. The agreement to negotiations in this area provide an important opportunity to advance simultaneously trade liberalization, environmental protection, and development goals.

The past year also marks an important turning point in the marshaling of government resources to deal with distortive foreign subsidies and other unfair trade practices, and in the intensity and focus of those efforts. A new, Administration-wide trade compliance initiative was launched in 2001, with additional personnel and resources throughout the Executive Branch being dedicated to increased monitoring and enforcement activity as concerns our trading partners' adherence to their bilateral and multilateral trade commitments. In terms of subsidies enforcement, the Administration has both expanded the reach and strengthened the organization of its resources as part of this broader trade compliance effort.

Last year, the Trade Remedy Compliance Staff was established within Commerce's Import Administration for the purpose of addressing the problem of foreign unfair trade practices, particularly those originating in East Asia, in a more pro-active fashion. Pursuant to Congressional directives, a staff of unfair trade analysts was assembled with exclusive responsibility for tracking and analyzing government policies, business practices and trade trends in China, Japan and Korea for possible evidence of burgeoning unfair trade problems. These Washington-based analysts will work in coordination with Trade Remedy Compliance officers posted in China, Japan and Korea in order to support administration of the U.S. unfair trade laws, monitor other countries' use of their own trade statutes, and work closely with U.S. industries in order to prevent and impede at an early stage the development of unfair trade problems that could both harm U.S. interests and create unnecessary frictions with our trading partners.

Nowhere is this more critical than with respect to China, whose accession to the WTO in December 2001 opens the door to increased and more predictable trading opportunities, but also presents challenges in terms of the need to work closely with the Chinese to ensure that they implement fully their WTO obligations. In this regard, the Trade Remedy Compliance Staff has been given important responsibilities within the Administration to lead the U.S. government's monitoring duties with respect to China's WTO accession commitments concerning subsidies and unfair trade remedies. In addition to these duties, this staff will continue to build upon its monitoring of Chinese industrial and economic policies and analysis of import trends. This will position the Administration to flag nascent problems and assist U.S. industries in exercising their rights under U.S. trade laws and special WTO safeguard mechanisms established uniquely in connection with China's accession.

The Administration has also aggressively employed its subsidies enforcement "infrastructure" during this past year to address the continued severe import competition faced by the U.S. steel industry. The Administration's comprehensive steel initiative consists of three parts: (1) a section 201 safeguards investigation of steel imports; (2) negotiations seeking the near-term elimination of inefficient excess capacity; and (3) longer-term negotiations aimed at strengthening the rules governing steel trade in order to eliminate the subsidies and underlying market-distorting practices that led to the current situation. Following the U.S. International Trade Commission's injury ruling

and remedy recommendation in the safeguard proceeding, the President is now evaluating the appropriate next step. We have had some constructive discussions in the OECD with respect to addressing the inefficient excess capacity problems facing the steel sector. Building on these discussions, we are now planning to move into the third prong of the initiative and address the underlying distortive practices. The mandate agreed upon at the WTO's Fourth Ministerial Conference in Doha, Qatar, to clarify and improve existing subsidy disciplines affords the United States the opportunity to execute the third prong of the Administration's initiative of effectively addressing the long-term market-distorting practices that have historically and intractably plagued the global steel industry.

As we move forward with a strong affirmative agenda in the WTO throughout the upcoming year, we will continue our monitoring, counseling and advocacy activities designed to serve the interests of those U.S. parties facing particular problems from subsidized competition. The fundamental aim of these activities is not to generate trade disputes or to punish or retaliate against subsidization, per se. While the United States will not shrink from exercising its internationally recognized rights to offset the effects of injurious, subsidized imports into the U.S. market, our underlying objective is to seek ways of addressing such problems without imposing yet more costs and obstacles to international commerce and investment. Thus, the objective of the subsidies enforcement program is to provide a pro-active tool to identify and root out subsidization that is demonstrably distortive of competition and the efficient allocation of economic resources. By addressing the problem of unfair subsidies at their source, whether through advocacy, negotiation or legal action, the Administration seeks to free efficient U.S. firms and workers from the burden of having to compete with foreign treasuries, to free U.S. taxpayers from the consequences of political pressure to compete with such subsidization, and to offer U.S. consumers and citizens the full range of choice, quality and affordable prices that can only be obtained through engagement in a dynamic and competitive global economy.

INTRODUCTION

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

With the enactment of the Uruguay Round Agreements Act (URAA) in 1994, the two agencies' roles were further articulated and mutually reinforced in order to facilitate the exercise of U.S. multilateral rights with respect to subsidies that harm the interests of U.S. firms and workers. Among the joint responsibilities assigned to USTR and Commerce, as set forth in section 281(f)(4) of the URAA, is the submission of an annual report to the Congress describing the Administration's monitoring and enforcement activities throughout the previous year. This report constitutes the seventh annual report to be transmitted to the Congress pursuant to this provision.

MONITORING AND ENFORCEMENT ACTIVITIES

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

The Agreement nominally divides subsidy practices among three classes: prohibited (red light) subsidies; permitted yet actionable (yellow light) subsidies; and permitted, non-actionable (green light) subsidies. Export subsidies and import substitution subsidies are prohibited. All other subsidies are permitted, yet are also actionable (through CVD or dispute settlement action) if they are (i) "specific", i.e., limited to a firm, industry or group thereof within the territory of a WTO Member and (ii) found to cause adverse trade effects, such as material injury to a domestic industry or serious prejudice to the trade interests of another WTO Member. Although originally three kinds of government assistance qualified as non-actionable, at present the only non-actionable subsidies are those which are not specific, as defined above. [\(1\)](#)

On the basis of these categories of discipline, the Subsidies Agreement provides remedies for subsidies affecting competition in one's domestic market, in the market of the subsidizing government and in third country markets. These disciplines serve as an important complement to the U.S. CVD law which is limited to addressing the effects of foreign subsidized competition in the United States. Although the procedures and remedies are different, the Subsidies Agreement provides an alternative tool to address distortive foreign subsidies that affect U.S. businesses and workers in an increasingly global marketplace. Within Commerce, these activities are carried out by Import Administration through the Subsidies Enforcement Office (SEO).

In 2001, the monitoring and enforcement activities of USTR and Commerce fell into the following categories: (A) pursuing and defending U.S. interests in the WTO, including in the ongoing work of the Subsidies Committee and the consideration of various subsidy-related implementation issues; (B) counseling the U.S. private sector and relevant government agencies about WTO subsidy disciplines; (C) establishment of a Trade Remedy Compliance Staff to both expand and deepen U.S. unfair trade monitoring and enforcement activities; (D) monitoring foreign subsidy practices and activities, including (i) foreign government support to the steel, semiconductors and cattle/beef industries, (ii) tracking of China's subsidy-related WTO accession commitments, and (iii) maintenance of the subsidies enforcement library; and (E) taking action to enforce U.S. rights and protect U.S. interests, ranging from WTO dispute settlement to formal and informal advocacy to assist U.S. firms, farmers and workers.

A. Activities in the WTO

Apart from individual WTO disputes, discussed more fully in section G. below, the WTO's focus in 2001 on general subsidies issues involved primarily three fora: the Committee on Subsidies and Countervailing Measures, the General Council and the Fourth Ministerial Conference.⁽²⁾ In the Subsidies Committee, the ongoing notification and review activities continued along with intensive discussions on various implementation issues. The United States' primary goal regarding the notification work of the Subsidies Committee continued to be the full and timely adherence by WTO Members with their subsidy obligations while being open to alternative approaches to lessen the burden of meeting certain notification obligations without diminishing their substance. While implementation issues were discussed in the Subsidies Committee, the Subsidies Agreement also featured prominently in the Special Sessions of the General Council on Implementation. The United States sought to work pragmatically to address legitimate implementation problems consistent with the policy, practice or legal framework of the United States' subsidy enforcement regime. In the WTO rules area generally, the United States secured a mandate at the Fourth Ministerial Conference to improve the disciplines under the Subsidy and Antidumping Agreements and address the trade-distorting practices that give rise to countervailing and dumping duties. Further information on these topics is detailed below.

1. Ongoing Work of the WTO Subsidies Committee

The Committee held two regular meetings in 2001. In addition to its normal activities concerned with reviewing and clarifying the consistency of WTO Members' domestic laws, regulations and actions with Agreement requirements, the Committee continued to accord special attention to the general matter of subsidy notifications and the process by which such notifications are made to and considered by the Subsidies Committee. In this regard, the Committee developed a strategy and took action to address the poor and declining state of compliance with subsidy notifications in an effort to find a long-term solution to the problem. Additionally, the United States at both formal meetings of the Committee expressed serious concerns regarding the financial assistance provided by the Korean government and state-owned banks to Korea's DRAM semiconductor industry. Finally, the Committee also selected a new member for its Permanent Group of Experts.⁽³⁾

a. Review of Subsidy Notifications

Subsidy notification and surveillance is one means by which the Subsidies Committee and its Members seek to ensure adherence to the disciplines of the Agreement. In some instances, notification is mandatory, while in others it is an optional feature that can be used to secure a benefit provided by the Agreement – such as to make use of transition periods during which a Member would come into conformity with Agreement norms. In keeping with the objectives and directives expressed in the URAA, and as demonstrated by the extensive use of the SEO's Electronic Subsidies Enforcement Library, WTO subsidy notifications also play an important role in the United States' monitoring and enforcement activities to protect U.S. rights and benefits under the Subsidies

Agreement.

Under Article 25.2 of the Agreement, Members are required to report certain information on all measures, practices and activities that, as set forth in Articles 1 and 2 of the Agreement, meet the definition of a subsidy and are specific within the territory of a Member. "New and full" notifications are submitted every third year, whereas updating notifications (usually containing information solely on changes made to previously notified subsidies) are submitted in the intervening years. Article 26 of the Agreement charges the Committee with reviewing the full notifications at special sessions held every third year, whereas updates are reviewed at regular, semi-annual Committee meetings.

In 2001, at its two regular meetings, the Committee continued its examination of new and full notifications submitted for 1998, as well as updating notifications submitted for 1999 and 2000. The table which follows shows the 21 Members (counting the European Union (EU) and its 15 member states as one) whose notifications were reviewed by the Subsidies Committee last year, indicating the annual reporting period to which the reviewed notifications relate.

WTO SUBSIDY NOTIFICATIONS REVIEWED IN 2001			
WTO MEMBER	1998 Full Notification	1999 Update Notification	2000 Update Notification
AUSTRALIA			X
BRAZIL		X	X
CUBA	X	X	X
CYPRUS		X	
DOMINICA		X	X
EU (incl. 15 member states)		X	X supplement
GHANA		X	
ISRAEL	X	X	X
JAMAICA		X	X
JAPAN			X supplement
LATVIA			X
MEXICO		X	X
NEW ZEALAND		X	X
NORWAY			X
PARAGUAY		X	X

POLAND			X
THAILAND		X	X
TUNISIA	X	X	X
TURKEY			X
UGANDA	X	X	X
ZAMBIA	X	X	X

As of January 1, 2002, when membership in the WTO had reached 144, only 50 Members had submitted new and full subsidy notifications for the 1998 reporting period, while 43 and 35 Members, respectively, had submitted updating notifications for the 1999 and 2000 periods. Notably, 41 Members have never made a subsidy notification to the WTO.

In view of the ongoing difficulties experienced by Members, including the United States,⁽⁴⁾ in meeting the Agreement's subsidy notification obligations, the Committee took several actions in 2001 aimed at improving the situation. At the end of 2000, the Working Party on Subsidy Notifications was reconvened to take a fresh look at the notification problems confronting Members and develop possible long-term solutions for the Committee's consideration. Following the review of Member information concerning the specific problems faced in making notifications and several informal meetings in the spring of 2001, a three-prong strategy was agreed upon to address the problems identified. The first prong was to examine alternative practical approaches to the frequency and nature of subsidy notifications, as well as their review. Examination of the subsidy notification format is the second prong of the strategy – that examination began in 2001 and will continue into 2002. The third prong is the organization of a subsidy notification seminar in the fall of 2002, coinciding with the regular Committee meeting, for government officials from developing countries responsible for notification.

Pursuant to this strategy, an important and practical step forward was taken by the Committee in 2001 with respect to the frequency and nature of subsidy notifications. As noted above, under Article 26 of the Agreement, "new and full notifications" are submitted every third year; while "updating notifications" are submitted in intervening years. At a special meeting held in May 2001, the Committee recognized that resource constraints were a leading reason for most Members' difficulties in submitting timely notifications. Indeed, Members indicated that the effort and resources required to prepare the annual updating notifications are essentially equal to those required for new and full notifications. Generally, Members considered that their resources would be best utilized by devoting maximum effort to submitting new and full notifications, every two years, and by de-emphasizing the review of the annual updating notifications. Under this new approach, Members can concentrate their resources in alternating years, first on making their own new and full notifications, and then on reviewing other Members' notifications. It is expected that this approach will have the effect of increasing transparency – the objective of the notification obligation under the Agreement – but will not add to or detract from Members' rights and obligations under the Agreement.

b. Other Activities of the Committee

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

To date, 88 Members of the WTO (counting the EU as one) have notified that they currently have CVD legislation in place, while 39 Members have notified that they maintain no such legislation. Among the notifications of CVD laws and regulations reviewed in 2001 were those of Burundi, Canada, Chile, Croatia, Ecuador, Jordan, Korea, Latvia, Malaysia, Morocco, Mexico, Oman, Peru and Tunisia. As for CVD measures, seven WTO Members notified CVD actions taken during the latter half of 2000, whereas seven Members also notified actions taken in the first half of 2001. The Committee reviewed actions taken by Argentina, Australia, Canada, the EU, Peru, South Africa and the United States.

c. Implementation Issues

An important feature since the outset of the WTO has been oversight by the General Council and the Committee on Trade in Goods of the implementation of WTO Agreements. In 2000, following up in part on concerns that had been raised by various WTO Members prior to and at the Third Ministerial Conference in Seattle in December 1999, the General Council agreed to conduct a special review of issues identified by Members as giving rise to implementation concerns under existing WTO Agreements. Numerous Special Sessions of the General Council and informal consultations among Members were held in 2001 in order to consider certain issues in greater depth and explore development of consensus-based approaches to problems. An inventory of specific concerns identified by certain developing countries prior to the Seattle Ministerial provided the benchmark for discussions, but the work was not limited to these concerns. The Council's purpose was to increase political attention and organize improved technical support towards the resolution of implementation issues; however, progress was difficult due to disagreements among Members over which issues were genuine problems of implementation and whether/how best to address them.

Various issues concerning the Subsidies Agreement figured prominently in the General Council's discussions. Many developing countries sought changes to the Agreement in an attempt at loosening disciplines applicable to them regarding the use of subsidies and lessening these countries' exposure to CVD actions. Some of the more extreme proposals advanced by various developing countries sought to: make export subsidies non-actionable when provided by a developing country; expand greatly the number of developing countries entitled to certain "special and differential treatment"

under the Subsidies Agreement; and modify CVD rules by, for example, raising the levels which establish de minimis rates of subsidization and negligible import volumes in cases involving developing countries.

The United States engaged actively and constructively in these discussions, but was clear about its goals and expectations. We indicated our readiness to work towards practical solutions for real implementation problems, but we expressed deep reservations regarding any proposal which might weaken the fundamental disciplines or conflict with the core objectives of the Subsidies Agreement. In short, the United States sought to ensure a process which would separate out and stress legitimate implementation issues from those which were actually aimed at a selective alteration in the terms of the Agreement. Therefore, the logical place to start, we argued, was for a serious and responsible examination of such issues in the Subsidies Committee without prejudice to the positions which Members might take as to the merits of such proposals.

Over the course of 2001 and especially during the lead-up to the Fourth Ministerial Conference, the Subsidies Committee held numerous informal and formal meetings to discuss several implementation issues. Pursuant to various General Council decisions, the Committee held extensive discussions on five general topics:

- determining "export competitiveness" under Articles 27.5 and 27.6 of the Agreement, including the possibility of extending the period for establishing export competitiveness;
- special procedures, under Article 27.4 of the Agreement, for small exporter developing countries seeking an extension of the transition period for the phase-out of export subsidies;
- the appropriate methodology for calculating the permissible level for rebates of indirect taxes and import duties on exported products pursuant to the Illustrative List of Export Subsidies found in Annex I of the Agreement;
- a general review of the Agreement's provisions regarding CVD investigations; and,
- the methodology for the calculation of the per capita GNP threshold delineated in Annex VII of the Agreement for the designation of certain developing countries entitled to particular types of "special and differential treatment" under the Agreement.

1. Determining "Export Competitiveness" under Articles 27.5 and 27.6

Under Article 27.2, developing countries not listed in Annex VII of the Agreement must phase-out their export subsidies no later than January 1, 2003. Notwithstanding this provision, Article 27.5 and 27.6 of the Agreement provide that a developing country which has reached 3.25 percent of world trade in a given product over two consecutive years must accelerate the phase-out of its export subsidies on that product. The product scope is defined as a section heading of the Harmonized

System nomenclature.

Many developing countries sought: (1) an extension of the period for establishing export competitiveness under Article 27.6 from two to five years; and, (2) a mechanism to allow developing countries that have achieved export competitiveness to resume export subsidization if exports fall below the level of export competitiveness. An expansion of the countries eligible for the special and differential treatment provided to Annex VII countries and a broadening of the product scope for the determination of export competitiveness were also sought. The United States expressed opposition to the various iterations of these proposals to the extent that they were contrary to the clear language of the Agreement or fostered the unjustified loosening of existing subsidy disciplines.

In the end, the Committee could not reach consensus on how the two-year period could be effectively extended without violating the express terms of the Agreement, or whether, the two-year period could be calculated on an alternative basis, such as a multi-year rolling average. As to the mechanism for the resumption of export subsidization after export competitiveness is lost, numerous issues remained unresolved as to the terms under which a resumption could be authorized. Nor was agreement reached regarding the appropriate level of aggregation under the Harmonized System nomenclature when defining the product scope and the expansion of the countries eligible for the special and differential treatment provided to Annex VII countries under the Agreement. This implementation proposal was eventually omitted from the Chairman of the General Council's draft proposed decision on implementation and was not considered at the Fourth Ministerial Conference.

2. Special Article 27.4 procedures for small exporter developing countries

As noted above, the Agreement requires developing countries to eliminate their export subsidies by the end of 2002. Article 27.4 of the Agreement allows for an extension of this deadline on a year-to-year basis if a request is made to the Subsidies Committee by December 31, 2001. Upon receipt of such a request, the Committee must decide whether an extension is justified based on relevant "economic, financial and development needs" of the developing country Member. If the Committee grants an extension, annual consultations with the Committee must be held to determine the necessity of maintaining the subsidies.⁽⁵⁾ If the Committee does not affirmatively sanction a continuation, the export subsidies must be phased out within two years.

Two developing country proposals were made early in the review process that would have permanently grandfathered the export subsidy programs of developing countries under certain conditions.⁽⁶⁾ One of the conditions proposed was that the exports of the developing country represent a small share of total world exports. Several countries, including the United States, objected to the proposed permanent exemption from the Agreement's export subsidy disciplines. Instead, the United States urged interested developing country Members to use the existing extension procedure set out in Article 27.4 of the Agreement. In an attempt to try and address the desire of certain "small exporter" developing countries for some measure of certainty in the extension process, a special procedure was discussed within the context of Article 27.4 of the Agreement under which countries

whose share of world exports was not more than 0.10 percent and whose Gross National Income was not greater than \$20 billion could be granted a limited extension for particular types of export subsidy programs subject to rigorous transparency and standstill provisions.

While the Committee could not reach a consensus on all the particular provisions of the extension procedure – such as the length of the extension – based on the Committee's work, the Committee chairman made a recommendation to the General Council which substantially formed the basis of the procedure agreed upon as part of the implementation decision taken at the Fourth Ministerial Conference. Members meeting all the qualifications for the agreed upon special procedures will be eligible for a five-year extension of the transition period, in addition to the two years referred to under Article 27.4.⁽⁷⁾ To date, Antigua and Barbuda, Barbados, Belize, Bolivia, Costa Rica, Dominica, the Dominican Republic, El Salvador, Grenada, Guatemala, Honduras, Jamaica, Jordan, Kenya, Mauritius, Panama, Papua New Guinea, St. Kitts and Nevis, St. Lucia, St. Vincent and Grenadines, Sri Lanka, Suriname, and Uruguay have applied for the special procedures under Article 27.4.⁽⁸⁾ The Committee will conduct a detailed review of all extension requests in 2002.

3. The appropriate methodology for the calculation of the rebate of indirect taxes and import duties

Under the Agreement's export subsidy rules, countries are permitted to rebate certain indirect taxes (e. g., sales taxes) and import duties on inputs consumed in the production of, or physically incorporated in an exported product. The Committee considered two implementation proposals with respect to this issue. The first was a request that countries be permitted to calculate the level of the rebate on an "aggregate" or "generalized" basis rather than on a product- or company-specific basis. Under such an approach, a particular rebate level would be established on an industry-wide basis and the same rate applied to each company in the industry. Due primarily to serious reservations – expressed by the United States and other developed country Members – that any aggregate methodology for calculating the rebate could result in an excessive rebate, no consensus was reached within the Committee on this point.

The second proposal related to the question of whether indirect taxes and import duties on capital equipment used in the production of exports could be included when calculating the amount of the rebate. As noted above, under the Agreement indirect taxes and import duties on inputs consumed in the production process can be rebated when a product is exported. However, the phrase "inputs consumed in the production process" as defined in the Agreement does not specifically include capital equipment. Due to the clarity of the language in the Agreement, many Members, including the United States, voiced concern that this was not an issue of implementation and that adoption of this proposal would effectively constitute as an amendment of the Agreement. Other countries expressed doubts as to how the rebate could be accurately and transparently calculated. Consequently, this proposal was not adopted.

4. Review of the provisions of the Agreement regarding countervailing duty investigations

The General Council referred this topic to the Committee on August 2, 2001. Brazil and India submitted papers making specific proposals as to how to clarify or, in some instances, modify the provisions of the Agreement regarding CVD investigations. The proposals related to: the appropriate definitions of "domestic industry" and "like product;" the use of "facts available;" numerous calculation issues; and the conduct of annual reviews of CVD orders already in place. Due to the breadth and complexity of the issues raised and the relatively short period of time prior to the Fourth Ministerial Conference, very little substantive discussion occurred beyond the formal presentation of these proposals. Thus, the Committee recommended to the General Council that the Committee continue to consider these issues. This recommendation was taken as part of the implementation decision taken at the Fourth Ministerial Conference.

In December of 2001, the Committee met and agreed upon a plan to examine and discuss the two previously submitted papers. The Committee must report to the General Council by July 31, 2002. However, in light of the anticipated rules negotiations, it is unclear the extent to which the Committee is the appropriate forum for addressing some of the proposals, especially those which impact the rights and obligations of countries under the existing Agreement.

5. The methodology for the calculation of the per capita GNP threshold in Annex VII of the Agreement

Annex VII of the Agreement identifies certain countries that are eligible for particular special and differential treatment. Specifically, the export subsidies of these countries are not prohibited and, therefore, are not actionable under the dispute settlement process.⁽⁹⁾ Secondly, a higher de minimis subsidy threshold applies in CVD investigations of imports from these countries, although this standard expires at the end of 2002.⁽¹⁰⁾

The countries identified in Annex VII include those WTO Members designated by the United Nations as "least-developed countries" (Annex VII(a)) as well as countries that had, at the time of the negotiation of the Agreement, a per capita GNP under \$1000 per annum and are specifically listed in Annex VII(b).⁽¹¹⁾ A country automatically "graduates" from Annex VII(b) status when its per capita GNP rises above the \$1000 threshold. When a country crosses this threshold it becomes subject to the subsidy disciplines applicable to other developing countries.

Since the entry into force of the Agreement in 1995, the de facto interpretation by the Committee of the \$1000 threshold has been that it is expressed in current (i.e., nominal or inflated) dollars. The concern with this interpretation, however, was that a country could graduate from Annex VII on the basis of inflation alone, rather than on the basis of real economic growth. As a reasonable alternative, the use of a \$1000 constant 1990 dollar threshold was first raised as part of the preparatory process for the Third Ministerial Conference in Seattle, and at that time some work on different possible methodologies for deriving GNP per capita in constant 1990 US dollars was developed.⁽¹²⁾

In October 2001, the Chairman of the General Council requested that the Committee take up the question of the methodology for calculation of the \$1000 threshold in constant 1990 US dollars. The Chairman of the Committee, in conjunction with the WTO Secretariat, developed an approach based on certain World Bank data that were used by the Uruguay Round negotiators in 1990 in developing Annex VII(b). While many Members expressed the view that they could accept this proposed methodology, other Members indicated that it was more appropriate to rely on more recently available data. Thus, it was not possible to reach a consensus on the question of methodology.

At the Fourth Ministerial Conference, it was agreed:

. . . that Annex VII(b) to the Agreement on Subsidies and Countervailing Measures includes the Members that are listed therein until their GNP per capita reaches US \$1,000 in constant 1990 dollars for three consecutive years. This decision will enter into effect upon the adoption by the Committee on Subsidies and Countervailing Measures of an appropriate methodology for calculating constant 1990 dollars. If, however, the Committee on Subsidies and Countervailing Measures does not reach a consensus agreement on an appropriate methodology by 1 January 2003, the methodology proposed by the Chairman of the Committee set forth in G/SCM/38, Appendix 2 shall be applied. A Member shall not leave Annex VII(b) so long as its GNP per capita in current dollars has not reached US \$1000 based upon the most recent data from the World Bank.⁽¹³⁾

Pursuant to this decision, the Committee will re-examine the methodology proposed by the Chairman of the Committee in the course of 2002.

In addition to the subsidy-related implementation issues noted above, the Fourth Ministerial Conference agreed to three other proposals made by the Chairman of the General Council.⁽¹⁴⁾ The first permits a Member whose GNP per capita rose above \$1000 and graduated from Annex VII to be re-included in Annex VII if its GNP per capita falls back below \$1000. This proposal addresses the concerns of some developing countries whose GNP per capita may have passed the \$1000 threshold at one point in time, but has since dropped below the threshold following a severe financial crisis or natural disaster. Indonesia's per capita GNP figure, for example, dropped several hundred dollars after the 1997-98 Asian financial crisis.

The second implementation proposal adopted reaffirms the rights of least- developed countries under the Agreement to provide export subsidies and to have an eight-year phase-out period for export subsidies after export competitiveness is reached with respect to a particular product.⁽¹⁵⁾ This proposal essentially restates existing provisions of the Agreement.

The third subsidy-related implementation action takes notes of a proposal to treat certain types of subsidies provided by developing countries as non-actionable and urges countries not to challenge the types of subsidies listed. A number of developing countries had sought to impose a moratorium on

WTO dispute settlement cases against the subsidies described. This was not acceptable to the United States and others. The hortatory language eventually agreed upon does not affect a country's ability to bring a CVD action under its national laws.

d. Doha Ministerial Declaration

At the Fourth Ministerial Conference, the United States secured a two-stage mandate to improve the disciplines under the Subsidies and Antidumping Agreements and address the trade-distorting practices that give rise to countervailing and antidumping duties. The mandate recognizes that the negotiations must preserve the basic concepts, principles and effectiveness of the two Agreements and that unfair trade laws are legitimate tools for addressing unfair trade practices that cause injury. Under this mandate, the United States will be able to pursue an aggressive, affirmative agenda, aimed at strengthening the rules and getting at the underlying causes of unfair trade practices.

The existing WTO disciplines on subsidies prohibit only two types of subsidies: industrial export subsidies and import substitution subsidies; other permitted subsidies, however, also distort markets and international trade patterns. The specific language of the mandate agreed to at the Fourth Ministerial Conference is critically important because it provides an avenue to address these other practices and to inform the discussions of subsidy and antidumping measures in a constructive manner. Moreover, it will provide an avenue to address subsidy concerns in key sectors of the U.S. economy. The Administration intends to consult widely in shaping its proposals in this important area.

The negotiating mandate will also permit the U.S. to include in its affirmative agenda proposals that will defend the legitimate interests of U.S. exporters, who are increasingly becoming subject to unfair trade cases abroad. While the Administration is developing proposals in this area, at a minimum, U.S. proposals can be expected to clarify and strengthen the rules on trade remedy procedures to ensure that the practices of other countries are as transparent and fair as those in the United States. This will enable U.S. exporters to compete abroad with the assurance that they will not be denied fundamental procedural due process protections.

An important accomplishment of the United States at the Fourth Ministerial Conference was the inclusion of fish subsidies as part of the rules negotiations. The United States has believed for some time that the depleted state of the world's fisheries is a major economic and environmental concern, and that subsidies that contribute to overcapacity or overfishing, or have other trade-distorting effects, are a significant part of the problem. As mentioned in previous reports, the United States, along with a number of other Members pressed for the initiation of negotiations on this topic at the Third Ministerial Conference meeting in Seattle. Building on this work, the United States made the initiation of negotiations aimed at eliminating harmful fish subsidies a major objective at the Doha Ministerial. The inclusion of fishery subsidies in the rules negotiations represents a significant opportunity for all countries to advance simultaneously the goals of trade liberalization, environmental protection, and economic development.

e. Areas of Focus in 2002

As discussed above, the development and presentation of an aggressive affirmative agenda for the rules negotiations will be the primary focus for the United States in 2002. As to the other WTO subsidy-related work, the Subsidies Committee will continue to cast its attention to implementation issues in a variety of respects. First, as a direct result of the implementation decision taken at the Fourth Ministerial Conference, the Committee will continue its examination of the provisions of the Agreement regarding CVD investigations and report to the General Council by July 31, 2002. Second, the United States will actively review the normal and special extension requests made under Article 27.4 of the Agreement to ensure the close adherence to the provisions of the Agreement and the agreed upon procedures for small exporter developing countries. Third, as noted, the United States will continue to work with others to try and identify ways to rationalize the burdens of subsidy notification for all WTO Members without diminishing transparency or taking away from the other substantive benefits of the notification obligation. Finally, the United States will continue to play a leading role in the review of other WTO Members' CVD legislation and actions, and will bring to Members' and the Committee's attention any concerns which may arise about such laws or actions, whether in general or in the context of specific proceedings.

B. Trade Compliance Initiative

The Administration's subsidy enforcement efforts received a substantial boost in 2001 with the launching of the U.S. Trade Compliance Initiative. This initiative provides substantial resources to several Executive Branch agencies for the purpose of intensifying U.S. monitoring of trade agreements and strengthening enforcement of U.S. trade laws. Increased attention to these activities will help to ensure that the United States reaps in full the expected benefits of the market-opening trade agreements to which it is a party, and to instill greater confidence in the value of expanded trade and competition to the U.S. economy and society.

As part of this trade compliance effort, Congress specifically directed that certain funds be used to base senior Import Administration personnel in several U.S. embassies, as well as to step up Import Administration surveillance and other activities to address more pro-actively unfair trade problems originating in some of our major trading partners, such as China, Japan and Korea. To achieve these goals, Commerce established the Trade Remedy Compliance Staff (TRCS) within Import Administration, which consists of a corps of senior officers to be posted in U.S. missions in such locations as Beijing, Tokyo and Seoul, as well as substantial additional personnel to augment Import Administration's existing import monitoring and subsidies enforcement activities. (See Attachment 1.) In line with Congress' priority, we have dedicated approximately half of these new hires to work on various activities and projects aimed at the identification and evaluation of potential unfair trade practices and policies in China, Japan and Korea.

The TRCS overseas officers, who will be arriving on station during 2002, provide a powerful new tool to enhance trade compliance and subsidy monitoring. As part of the Administration's efforts to

measure and assure foreign compliance with trade obligations, these officers will assist and offer expert technical support to U.S. Foreign Service and Foreign Commercial Service officers in order to better identify, collect, assess and confirm information about market conditions, trade practices and government policies in the host country that may contribute to or exacerbate the development of unfair trade problems with the United States. At the same time, the TRCS team in Washington will monitor U.S. imports and information regarding other countries' trade practices and government policies available from U.S. and other sources. By having its overseas officers interact with Import Administration analysts in Washington that are similarly tracking such conditions, practices and policies, Commerce intends for this initiative to serve as an important new resource to facilitate the application of U.S. unfair trade remedies, the correction of foreign practices and policies that lead to unfair trade, and the reduction of disputes that heighten trade frictions.

Given their proximity to host government officials and to businesses in the host country, the officers also have a variety of responsibilities related directly to the administration of the U.S. antidumping (AD)/CVD laws. As needed by Import Administration headquarters, the TRCS officers stationed overseas will present questionnaires to foreign firms and governments in AD/CVD investigations and administrative reviews; verify or facilitate the verification of responses to such questionnaires; provide technical support for the negotiation and monitoring of suspension agreements or other kinds of settlements of AD/CVD proceedings; assist in the identification, analysis and handling of circumvention allegations concerning AD/CVD measures; and serve as an in-country source of guidance and information for host-country firms participating in such investigations and reviews.

Beyond these duties, both the overseas officers and the Washington-based staff will help explain the U.S. system of unfair trade law enforcement to the foreign audience, whether that be government officials, business representatives, or other interested groups. This will promote better understanding of U.S. unfair trade policies, assist foreign firms in avoiding unfair trade problems with the United States, and encourage fuller and more effective participation in U.S. investigations and administrative reviews – a development which should mutually benefit the foreign parties and U.S. investigators, and generally improve the quality of investigative results. The expertise of TRCS personnel will also be used to more closely monitor the foreign government's use of unfair trade remedies, especially in situations affecting U.S. exporters, and to offer technical assistance to that government's authorities in an effort to enhance their transparency and respect for due process in applying WTO-sanctioned trade remedies.

C. China's WTO Accession: U.S. Monitoring of Subsidy-Related Commitments

On December 11, 2001, after approximately 15 years of negotiation, the People's Republic of China became the 143rd Member of the WTO. China's accession protocol and the report of the accession working party outline a lengthy and diverse range of commitments that China has made as part of its accession, reflecting both the importance of China as a trading power as well as its transitional status between a centrally planned economy and a more market-driven economic system. In a number of instances, these commitments require China to take a specific, affirmative action by a date certain, while others involve an ongoing obligation for China to adhere to certain rules in the conduct of its

trade regime. With regard to subsidies, China committed to the following:

- Upon accession, to eliminate all subsidies contingent upon export performance ("export subsidies") and all subsidies contingent upon the use of domestic over imported goods ("import substitution subsidies"). These are subsidies which are generally prohibited under Article 3 of the Subsidies Agreement.
- To ensure that any assistance provided by the government to minority autonomous regions and other areas of economic poverty will comply with China's WTO obligations;
- Not to seek to invoke certain provisions of the Subsidies Agreement that are intended to provide developing countries greater latitude in the use of subsidies (i.e., Articles 27.8 and 27.9, dealing with the application of the Agreement's multilateral actionable subsidy remedies to subsidies used by developing countries, and Article 27.13, concerning the limited exemption of certain privatization subsidies from challenge under those same multilateral remedies).
- To accept treatment of state-owned enterprises (including banks) as the "government" for purposes of determining whether or not financial assistance provided by such entities is a subsidy;
- To accept treatment of subsidies provided to state-owned enterprises as "specific" (and, therefore, potentially actionable under WTO rules or countervailable under national law⁽¹⁶⁾) if such enterprises are the predominant recipients of such subsidies or if they receive disproportionately large amounts of such aid; and
- To notify the WTO about all subsidies maintained within its economy, irrespective of whether such subsidies are specific.

Given China's role as a major U.S. trading partner and the breadth and complexity of its WTO commitments, the Administration has planned extensively to institute a comprehensive monitoring and enforcement program. USTR's Office of China has lead responsibility for overall interagency coordination of this effort, but the principal role for monitoring and analyzing compliance with China's subsidy commitments belongs to Import Administration and, in particular, its Trade Remedy Compliance Staff (TRCS) in the Office of Policy (see section B above).

The TRCS is well suited to undertake this task, given its ability to draw upon the technical expertise on subsidy matters residing within Import Administration and to call upon on-the-ground assistance from Import Administration's trade compliance officers that will be stationed in Beijing. In addition to monitoring China's prohibited subsidy phase-out obligations, the TRCS will also focus its monitoring activities on particular sectors where Chinese government intervention may be of special concern for U.S. industries, such as steel, and on larger developments in Chinese government policies

and market conditions that could influence the extent to which subsidization may occur. Private sector groups, including U.S. business associations, can provide important input and guidance to these efforts by identifying priority areas for monitoring and by sharing information and advice from their members. Like the SEO, the TRCS intends through this report and other means to increase the U.S. trading community's awareness of the resources it has to offer, and to reach out to interested groups in order to provide useful information, advice and options about how to address pro-actively subsidy and other unfair trade-related problems that may arise in our trade with China.

Another outlet for the work of the TRCS will be in the United States' participation in the so-called Transitional Review Mechanism. This mechanism was established uniquely for the purposes of China's accession, to provide China and other WTO Members the opportunity to exchange questions, answers and supporting information regarding China's compliance with its commitments. Each year over the next eight years (with a final review in year 10), the review will be conducted initially in 16 subsidiary WTO bodies, including the Subsidies Committee. These bodies will address implementation matters within their respective mandates and report the results of their reviews to the WTO's General Council, which will then conduct its own review and has the right to make recommendations to China based on the results of that review.

The United States is committed to keeping a close eye on the state of compliance by China in this critical area of WTO rules and disciplines. Should the Administration identify any subsidy-related compliance problems in connection with China's accession, it will act quickly to resolve them through all available and appropriate mechanisms.

D. The President's Steel Initiative

In furthering the Administration's goal of establishing an open, competitive global trading environment for U.S. exporters, the Administration looks to see if it can resolve issues faced by various industries that have experienced repeated trade problems over the years. The U.S. steel industry is one such industry and, therefore, continued to be a major focus of subsidies enforcement activity during the past year.

Although imports began to subside in 2001, record import levels over the last three years resulted in increased inventories and sharp price declines. With prices at an all time low, and capacity utilization dropping at times below 70 percent, the domestic steel industry suffered severe financial difficulties. By the end of 2001, more than a quarter of U.S. steel companies were in bankruptcy, and steelmaking capacity was reduced by almost 15 percent.

In an effort to address the ongoing crisis in the U.S. steel industry, on June 5, 2001, President Bush announced a comprehensive steel initiative. This steel initiative consisted of three parts:

- A request to the International Trade Commission to initiate a section 201 safeguards investigation of steel imports into the United States;

- Immediate negotiations seeking the near-term elimination of inefficient excess capacity in the global steel industry; and
- Longer-term negotiations aimed at strengthening the rules governing steel trade in order to eliminate the subsidies and underlying market-distorting practices that led to the current situation.

The goal of the President's steel initiative was twofold – first, provide the U.S. steel industry with the time needed to recover from the current crisis and allow U.S. industry to enhance its competitiveness, and second, return to market principles and eliminate the underlying structural problems that have continuously plagued this industry, viz., excess inefficient steelmaking capacity and a 50-year legacy of government subsidies and other market distorting practices.

1. Section 201 Investigation

On June 22, 2001, the Administration requested that the International Trade Commission initiate a section 201 investigation on steel. The request covered four broad categories of steel products – carbon and alloy flat-rolled steel, carbon and alloy long products, carbon and alloy pipe and tube, and certain stainless steel and tool steel products – that encompassed virtually all steel imports.⁽¹⁷⁾

In October 2001, the ITC made affirmative injury determinations with respect to imports of 16 product categories, covering roughly 74 percent of the steel products listed in the Administration's request.⁽¹⁸⁾ In December 2001, the ITC submitted remedy recommendations to the President regarding those products on which it found injury. The commissioners issued a broad range of recommendations. Most commissioners focused on tariff increases but some of the commissioners did recommend quotas or tariff-rate quotas for certain product categories. The Administration is currently evaluating the commissioners' recommendations, along with input from the domestic industry, steel consumers and other interested parties. The President is currently scheduled to announce his decisions stemming from the investigation in March 2002.

2. OECD Capacity Reduction Talks

The first high-level meeting on steel capacity reductions was convened at the OECD in September 2001. This meeting was extraordinarily successful – 39 major steel-producing countries, including non-OECD members, agreed that inefficient excess steel production capacity is a significant global problem for the steel industry.⁽¹⁹⁾ Furthermore, all of the participating countries agreed that governments should aggressively encourage the elimination of inefficient excess capacity.

As a next step toward achieving that goal, the participating countries agreed to consult with their respective steel industries and conduct a self-examination that defined and identified inefficient capacity, along with the social, economic and regulatory issues that might impede the closure or reduction of excess capacity. The findings of their self-assessments, including projections of future changes in capacity and potential policies in the short-term to encourage the reduction of inefficient excess capacity, were presented at a follow-up high-level meeting in December.

Because countries reported their findings on different time series that made comparisons difficult and not all of the countries submitted information on their respective steel industries, the participating countries agreed to meet again at the beginning of February, 2002, revise their findings in order to place them on a consistent basis for comparison, and discuss other new information, as well as to discuss the means to address those market-distorting practices which are the root cause of excess capacity. In addition, another meeting will be held in April, 2002 to further develop the high-level group's work on the issue of the reduction of excess capacity and explore measures to address the market-distorting practices that have led to the current condition of the industry.

3. Increased Disciplines on Steel Trade

Last year's Subsidies Enforcement Report to Congress provided an overview of Commerce's July 2000 "Report to the President on Global Steel Trade" which documented subsidy and market-distorting practices in major steel producing countries. Over time, subsidies and other types of government support helped to create and maintain capacity. Although, many types of direct support have diminished in recent years, they continue to be a concern in certain countries, particularly those that are recent entrants to global steel trade. In addition, indirect support and other types of market distorting practices also facilitate the maintenance of inefficient excess capacity.

The underlying factors contributing to global excess capacity generally fall into the following categories: (1) government subsidization, such as grants, debt forgiveness and provision of cheap inputs, (2) unsound bank lending practices, (3) flawed bankruptcy regimes, (4) lack of economic reform and normal business practices (in nonmarket economies and economies in transition), (5) cartel-like behavior among steel companies within the same country, (6) apparent arrangements between steel producers in different countries directing the flow of steel, and (7) import barriers, such as high import tariffs and taxes. These types of practices have often been cited by industry experts as contributing the most to the global overcapacity problem and, thus, will be the focus of our efforts during the next year. An integral part of the President's steel initiative is to negotiate rules that will govern steel trade in the future, ensure their effective enforcement and eliminate the underlying market-distorting subsidies that led to the current conditions.

E. Subsidies Enforcement Counseling and Outreach

During 2001, USTR and Commerce continued their efforts to strongly enforce the Subsidies Agreement in the advancement and protection of U.S. interests. The goal of the subsidies enforcement program is to provide a pro-active tool to identify and root out subsidization that is demonstrably distortive of competition and the efficient allocation of economic resources. By addressing the problem of unfair subsidies at their source, whether through advocacy, negotiation or legal action, the Administration seeks to establish a dynamic and competitive global environment for U.S. firms and workers.

Commerce's Subsidies Enforcement Office (SEO) is a key player in these efforts, responding directly to U.S. industry complaints and concerns about foreign subsidy practices. The SEO examines these complaints to determine whether the alleged subsidy practices harm U.S. companies and are inconsistent with the Subsidies Agreement. In support of this mission, the SEO has added considerable resources in 2001. These have significantly enhanced the SEO's ability to assist the private sector with their subsidy-related concerns. New resources have also been dedicated to the SEO's ongoing efforts to monitor, develop and analyze key information about foreign subsidy practices, integrate other government resources into this information gathering and advocacy process, and make all of its publicly available information about foreign subsidies Internet-accessible. An overview of all of these efforts is provided below.

1. Enforcement Counseling

USTR and Commerce SEO staff regularly respond to inquiries and meet with representatives of U.S. industries concerned with the subsidization of foreign competitors. Our goal is to resolve these issues through a combination of formal and informal contacts with foreign governments. However, if appropriate, we will also advise U.S. companies of other remedies, including, where warranted, CVD cases or dispute settlement actions in the WTO.

Enforcement counseling frequently starts with an inquiry by a U.S. exporter regarding a subsidy problem. Over the past year, we received a number of these inquiries and as a result we are currently counseling and advocating on behalf of a number of U.S. exporters. The type of inquiries and information provided by U.S. companies to the agencies through these contacts vary greatly. Some are simple questions concerning the Subsidies Agreement and U.S. rights under this Agreement. Others involve detailed complaints concerning specific subsidy practices and allegations that these practices have adversely affected U.S. companies, either in the United States or in foreign markets. In these cases, our staff discuss the subsidy problem with the exporter and then gathers information about the practice and how the company's ability to sell in the United States or foreign markets has been affected.

The firm or industry in question is usually the best source of information concerning the harm resulting from the subsidization. This information is critical to support a claim of "serious

prejudice," which is normally the most useful injury standard available in a WTO subsidy enforcement proceeding.⁽²⁰⁾ In most cases, we also conduct significant additional research to determine the legal framework under which the foreign government is offering the assistance and whether other U.S. exporters have been facing similar problems.

The sources we draw on to develop as much information as possible about the subsidy practice include a wide range of internal and external sources. We start with general sources such as the SEO's Electronic Subsidies Library, the Internet and news organizations. Discussions with other Commerce offices that routinely collect information on specific country and industry practices, and Commerce's Advocacy Center⁽²¹⁾ are also useful to learn whether any U.S. exporters have reported facing similar problems. If necessary, we will contact the U.S. embassy in the appropriate foreign country to discuss our findings and determine whether there is additional information that U.S. posts abroad can provide. It has also been useful to contact our counterparts in foreign governments to learn whether similar complaints about the same third-country subsidy practice have been identified by their exporters. Where appropriate, we may also seek public comment and/or consult with representatives of U.S. state and local governments.

Working with an interagency team, USTR and Commerce will then evaluate the information and determine the most effective way to proceed. As noted above, we have found that it is often advantageous to pursue resolution of these problems through a combination of informal and formal contacts. For example, raising the matter with the foreign government authorities through informal contacts, formal bilateral meetings and/or through discussions in the WTO Subsidies Committee may produce more expeditious and practical solutions to the problem than resorting to WTO dispute settlement. These contacts may lead to additional information about the practice, which can affect the decision concerning the appropriate measures to take, including the possibility of pursuing the problem on grounds other than those provided for under WTO subsidy rules. However, if these efforts fail to bring a resolution to the issue, bringing a formal dispute settlement action in the WTO remains a viable option for some cases.

2. Integration of Government Resources

The SEO conducts frequent outreach programs to ensure that government personnel who have daily contact with the U.S. exporting community, both in the United States and abroad, are aware of the resources and services available regarding subsidy enforcement efforts. Within Commerce, the U.S. Commercial Service (USCS) is charged with counseling U.S. companies through their network of domestic and foreign posts. SEO staff therefore hold formal briefings with USCS officers on rotation in Washington to explain the type of services and information offered by the SEO. We also provide USCS officers with handouts detailing SEO activities and contact information. These are used by the officers at their overseas posts to inform other USCS officers and visitors from the U.S. business community about our resources (See

Attachment 2.) SEO staff also benefit from information provided by USCS officers during these briefings about the types of subsidy problems U.S. companies are facing in the host countries. In addition, SEO personnel participate in special conferences for senior commercial officers and training sessions held for foreign service national employees⁽²²⁾ in Washington. These meetings allow SEO staff to inform a large number of government officials who have daily interaction with U.S. companies about the resources the SEO can offer.

As part of our ongoing outreach efforts, SEO personnel participated in a program sponsored by the Commercial Law Development Program (CLDP)⁽²³⁾ in Rabat, Morocco to provide technical assistance to Morocco's Ministry of Commerce as it developed trade remedy laws to address unfair trade practices. A major focus of the training program was an intensive analysis of the Subsidies Agreement. Included were in-depth discussions of procedural issues involving the administration of a trade remedies office, the timing and scope of investigations into unfair trading practices and the analysis of information. Calculation methodologies and procedures for identifying and evaluating foreign subsidy practices were reviewed. The training activities form part of a comprehensive program to strengthen ties between foreign officials and their U.S. counterparts, and help ensure that the administration of trade remedy laws by our trading partners are consistent with their international obligations.

The SEO also works closely with the U.S. Department of State to involve foreign service economic officers in subsidies enforcement activities. This fulfills our statutory mandate to secure the cooperation of other federal agencies in these activities, as provided for in section 281(g) of the URAA. To this end, USTR and SEO personnel have been training State Department economic officers on how to identify and evaluate foreign subsidy practices that may be inconsistent with the Subsidies Agreement and that may involve unfair trade actions against U.S. companies. Cooperation of this type occurs not only in specific cases initiated by the SEO or USTR, but on an ongoing basis whereby State Department economic officers develop and share information with Commerce, USTR and the interagency team concerning foreign government subsidy practices and the administration of foreign governments' unfair trade laws.⁽²⁴⁾ This type of collaboration between our Departments is critically important to help effectively enforce the Subsidies Agreement.

In 2001, we have maintained and extended our contacts and outreach efforts with U.S. embassies and consulates. The trade compliance and market access initiative has become operational, and the first steps toward placing personnel in posts abroad to enhance the effectiveness of U.S. monitoring and compliance of trade agreements, including the Subsidies Agreement, have been taken. (See section B above.) We also continued to meet with foreign service officers at a number of U.S. embassies and consulates in 2001, reinforcing the priority the Administration attaches to cooperation among government agencies towards effective enforcement of subsidies disciplines. During these meetings, we provided foreign service officers with information on WTO subsidy disciplines and the resources available through the SEO.

Embassy-based personnel offer a unique perspective to our subsidy enforcement efforts. USCS officers have daily contact with the U.S. exporting community and, therefore, are directly aware of the problems facing the companies. State Department economic officers often have key insights about the types of subsidy programs being administered, implemented or contemplated by the host governments. The type of information provided by U.S. Embassy staff has proven to be very useful in determining the most appropriate areas in which to focus our efforts to assist U.S. exporters.

SEO staff also maintain close contacts within Commerce's International Trade Administration (ITA), in particular the country and industry desk officers, the Advocacy and Trade Compliance Centers, and the Compliance Coordinators group (CCG). The Compliance Coordinators group is comprised of representatives from all of ITA's units (Market Access and Compliance, Trade Development, Import Administration, and USCS) and the Patent and Trademark Office, and serves as the central coordinating point for ITA's market access and agreement compliance activities. The group meets regularly to share information on trade compliance and market access issues that may be common across regions or industrial sectors, and works to resolve these issues by drawing upon the full range of expertise available within ITA. These contacts allow us to ensure that these offices are fully apprised of the SEO's subsidy enforcement activities and that they provide SEO staff with information that they routinely collect.

An example of the collaborative effort within ITA on subsidies enforcement is the SEO's work with the TCC and the Advocacy Center. The TCC monitors compliance with active international agreements covering manufactured goods and services to which the United States is a signatory. Complaints received by the TCC that may involve foreign subsidies are immediately referred to the SEO for analysis and action. The Advocacy Center assists U.S. exporters seeking government contracts abroad by providing U.S. government advocacy on behalf of the U.S. company when foreign competitors bidding on the same contract enjoy support from their governments. At times, this foreign government support may be in the form of subsidies. When the Advocacy Center receives a call from a U.S. company concerning possible foreign government subsidization, the Center contacts the SEO and provides all of the relevant information. In addition, the Advocacy Center has connected the SEO to its computer database. This allows us to review information gathered by the Center to determine whether U.S. exporters' access to foreign contracts is being impeded by government practices which may be actionable under subsidy rules.

F. Monitoring Foreign Subsidy Practices

1. Monitoring Subsidy Practices Worldwide

One of the primary missions of the SEO is to monitor subsidy practices worldwide. Towards this end, we have continued to expand our comprehensive database of foreign government

practices that are potentially actionable under the Subsidies Agreement. This information is made available to the public through the Internet on Import Administration's home page. The Internet provides an easy and efficient avenue to reach U.S. businesses and other interested parties in order to furnish them with information previously available only in person in Washington. This allows U.S. exporters to learn quickly about the remedies available to them under the Subsidies Agreement and to obtain the information necessary to develop a CVD case or a WTO subsidies complaint.

We reported last year that the SEO's electronic subsidies database was fully installed in 2000. We anticipated being able to update the subsidies library database on only a quarterly basis; however, fortunately, resources have been sufficient to enable us to update the database monthly. Therefore, information on subsidy programs investigated or reviewed by Commerce is quickly available to the U.S. trading community. We will continue our efforts to ensure that information is quickly and accurately added to the database so it is easily available to the public. The site, which can be found at <http://ia.ita.doc.gov/esel/eselframes.html>, includes information on all the foreign subsidy programs that have been investigated in U.S. CVD cases since 1980, covering more than 50 countries and over 2,000 government practices. Attachment 3 shows the layout of the library and includes the list of U.S. trading partners about which information is available on the site.

The Subsidies Enforcement and Import Administration sites also provide access to derestricted WTO subsidy notifications, listed by country, and easily accessible links to other useful U.S. and foreign government sites, such as USTR, the U.S. Ex-Im Bank, the IMF, the WTO (which maintains databases of Members' CVD actions, as well as their subsidy notifications to the WTO), the Canadian and Mexican government trade agencies, and the NAFTA secretariat. We are continuing our efforts to increase the number of useful U.S. government and foreign links provided. Another advantage to integrating all of the subsidy information developed through years of conducting CVD investigations and subsidy information provided to the WTO is that USTR and SEO staff can easily check the WTO subsidy notifications of other countries and ensure that they are complete and accurate. As discussed in Section A of this report, the notification process is an important aspect of our subsidy enforcement efforts.

Finally, during 2001, SEO staff have been engaged in several focused areas of work concerning subsidy practices in various countries affecting specific industries in the United States. An overview of these efforts is provided below.

2. Update – Government Aid Programs Potentially Benefitting the Cattle and Beef Industries

In response to a request made by several Senators in 2000, the SEO conducted a study of possible subsidy programs available to cattle and beef producers in a number of countries. The report, appended to last year's subsidies enforcement report to the Congress, examined

potential subsidies and other aid programs provided to foreign cattle and beef producers in the following countries: Argentina, Australia, Brazil, China, the EU, Japan, Korea, New Zealand, and Uruguay. In light of the continued importance this sector plays in the U.S. economy, and because updated information will help prepare for trade negotiations, the SEO continued its efforts on behalf of the U.S. cattle and beef industry in 2001.

This past year, the SEO followed developments related to potential subsidy practices in several major cattle and beef trading countries which may unfairly enhance exports from those countries into the U.S. market or work to impede market access abroad for U.S. cattle and beef exports. SEO personnel also met with industry representatives and shared last year's findings with the Ranchers-Cattlemen Action Legal Fund (R-CALF) at their annual convention in 2001. SEO staff intend to continue monitoring the changing trade situation and provide information to government and industry groups. It should be noted that mention of a government aid program in this update in no way prejudices the status of that measure under WTO rules and/or whether it is addressable under those rules or U.S. law.

The fed-cattle industry in the United States remains the largest in the world, and many of the production and consumption trends identified in last year's report continue. In 2001, the United States remained a net beef importer on a volume basis, with Canada providing the largest source of U.S. beef imports, followed by Australia. The United States also imports significantly more cattle than it exports. Beef imports have remained relatively stable, while exports, which had recently been growing strongly, lagged behind the record pace set in 2000. Red meat exports are expected to decline 3 to 4 percent in 2002.⁽²⁵⁾ Beef exports did, however, still account for approximately 12 percent of the value of wholesale U.S. beef sales. For live cattle, imports increased steadily over the past decade, and more quickly over the past year, while exports showed only moderate increases, although recent growth is evident. Several factors contributed to changes in traditional trade patterns that will affect U.S. beef and cattle imports and exports in the year ahead.

a. Argentina

Two major developments in 2001 have left Argentine beef and cattle trade in a state of uncertainty. First, in mid-March, 2001, Argentina announced the presence of foot and mouth disease (FMD). Over the next few weeks, over 300 hundred outbreaks were reported throughout Argentina's major cattle producing regions.⁽²⁶⁾ In response to the outbreak, exports of fresh, chilled, and frozen beef were suspended to the United States and many other markets. The Argentine Government has chosen to fight FMD through vaccination, which will result in the U.S. market remaining closed to Argentina's fresh beef exports for several years. Argentina's exports of cooked frozen and corned beef to the United States remain largely unaffected by the crisis. The European Union also remained closed to Argentine beef exports through December 2001. Although the EU approved a limited resumption of fresh beef imports from Argentina in mid-January 2002, Argentine exports are not expected to rebound

fully in 2002. U.S. short-rib and sweetbread exports to Argentina continued to grow in 2001, and U.S. exporters have an opportunity to improve their market share in third-country markets as a result of the closure of those markets to Argentine exports.

The second major development is still unfolding. Argentina's decision this January to allow its currency to float under most circumstances will likely make Argentine exports more competitive with Brazil's and may increase exports generally. However, the poor financial situation of many exporting firms, along with an increased dollar-denominated debt burden and the lingering effects of the FMD outbreak, will dampen any initiatives to increase export production capacity to take advantage of any potential exchange rate benefits.

Several measures were announced in 2001 to assist export packers affected by these problems. Most of the measures involve disease control and vaccination costs, financing working capital requirements, and tax advantages aimed at beef exporters. SEO staff also researched several programs identified in last year's report that required further analysis. Among those, the Reintegro tax rebate system was examined closely in 2001, in conjunction with an unrelated CVD investigation on honey, and found to be a countervailable subsidy. However, the Argentine Government announced the elimination of most Reintegro export reimbursements in June, and the establishment of a special exchange rate conversion factor system to benefit exporters.⁽²⁷⁾ Although reports indicate that the government reinstated export rebates in September, the changes to Reintegro and the adoption of the conversion factor were expected to have a minimal impact for exporters.⁽²⁸⁾ Finally, efforts to finalize legislation related to the creation of a Beef Promotion Institute are ongoing.

b. Australia

Australian exports comprise over one third of all U.S. beef imports, and Australia's total beef exports to the United States have increased steadily over the past year. Between January and October, 2001, the United States imported 26 percent more beef than during the same period in 2000.⁽²⁹⁾ The Foreign Agricultural Service (FAS) reports that small production increases are likely in 2001 and 2002. A favorable exchange rate, coupled with a lack of animal health concerns, should ensure growing exports in 2002; however, Australia's beef exports to the United States are subject to a tariff rate quota (TRQ). Australian beef exports compete with U.S. exports in Japan and Korea as well. Australia is also a major exporter of live cattle, primarily to Indonesia, the Philippines, and Egypt.

Meat and Livestock Australia (MLA), a producer levy-funded entity established by Australian law, worked with the Australian government to develop a cattle identification system that provides for full traceability and will enhance market access for exports. The system will be administered by a joint industry government initiative.⁽³⁰⁾ SEO staff monitored MLA's other marketing and research and development initiatives as well. State government programs identified last year, such as the New South Wales Regional Business Development Scheme,

potentially remain available to Australian beef producers.

c. Brazil

Brazil is a major beef-producing country, with a cattle population exceeding that of the United States by over 40 million head. Production is forecast to increase by four percent in 2002.⁽³¹⁾ Despite an outbreak of FMD in Rio Grande do Sul in May 2001, beef exports continued to grow strongly in 2001. This was due to the health measures instituted to confine the outbreak, new market opportunities resulting from suspensions of exports from Argentina and Uruguay, and the competitive advantage of Brazil's currency. The export growth trend is expected to continue. Brazil maintained its position as a major exporter of processed beef to the United States in 2001, despite a temporary ban on imports imposed by members of NAFTA following Canada's decision to halt imports due to animal health concerns. U.S. cattle and beef exports to Brazil are minimal, although exports of bovine genetics remain strong.

Several support programs are available under the 2001/2002 Crop Year Agriculture and Livestock Plan. The PROPASTO program, with total funding of \$166 million dollars, allows individual livestock producers to borrow up to \$63,000 at a below-market fixed rate of 8.75 percent. Additional subsidized credit is available for the building or repair of silos and warehouses on farms and for agricultural machinery modernization.⁽³²⁾ The Government also supported the creation of a market promotion program for Brazilian beef. The program seeks to create a "Brazilian Beef" brand, along with specialized marketing for organic beef and veal. The Brazilian Agriculture Ministry will provide \$500,000 dollars for export-related promotional activities through September 2002.⁽³³⁾

SEO staff continued to research financial assistance to the cattle and beef industry provided through the National Bank for Economic and Social Development (BNDES). Over the past year, reports indicate that BNDES has increased its financial support of meat products exports. BNDES loans, which carry interest rates of approximately 8 percent and generally have extended grace periods, are aimed at boosting productivity. Approximately \$10.5 billion, or 15 percent of the banks total financing, went to Brazil's agricultural sector in the 1990s.⁽³⁴⁾ BNDES also offers specialized financing assistance to meat packing firms through the FINAME program.

SEO staff also monitored regional support programs such as the Fundo de Investimento da Amazônia (FINAM) and Fundo de Investimento do Nordeste (FINOR), as well as programs administered by SUDAM/SUDENE, which all provide regional financial support.⁽³⁵⁾ The programs include provisions for income tax exemptions, reductions and tax cuts for reinvestment and are available to industrial and agricultural enterprises located in targeted regions.

d. European Union

European cattle and beef production and trade were disrupted by both bovine spongiform encephalopathy (BSE or "mad cow disease") and FMD outbreaks throughout 2001. In February 2001, Britain announced an outbreak of FMD that decimated part of the country's cattle herd and spread throughout much of the European Union, causing widespread economic disruption to the cattle and beef industries. As of November 2001, beef consumption in the EU was down 5.3 percent, but is expected to recover, along with production, in 2002. The Foreign Agricultural Service (FAS) forecasts a rebound in beef exports in 2002, as important markets such as Egypt reopen to European beef products.⁽³⁶⁾

The Community-wide programs identified in last year's report still provide support to the cattle and beef industries. The European Commission also amended its regulations regarding the advance payment rates for many of these support programs, which were increased from 60 percent to 80 percent of the full premium. Several programs were included in the EU's most recent WTO subsidy notification. The Price Support Regime remains unchanged, as do programs for young male bovine animals and maintenance of suckler cow herds. Additionally, a Slaughter Premium provides EUR 50 per calf and EUR 80 for adult cattle in 2002.⁽³⁷⁾

In addition to the subsidies previously identified, the EU and its Member States announced several exceptional measures to deal with the FMD and BSE outbreaks. It is estimated that approximately 478 million Euros were spent on Income Aid related to the animal health crisis and an additional 547 million Euros on other measures such as the Purchase for Destruction Scheme. The Scheme, which was funded primarily by the EU, expired in June 2001. More generally, the EU expects to conduct a mid-year review of its Common Agricultural Policy in 2003, although there are indications that these and other subsidies, such as export rebates and subsidies, will not be significantly reformed before 2005. Agricultural subsidy issues were an important part of the negotiations on EU enlargement that proceeded with several countries in 2001.

The SEO also followed reported allegations that French cattle producers and packers colluded to fix prices by not buying imported beef. Although the French government denied any involvement in the initiative, the European Commission launched an enquiry in early 2002 to determine whether any additional aid was released by the French government as part of the agreement.⁽³⁸⁾ Finally, the French Minister of Agriculture and Fisheries announced on January 7, 2002, a new \$134 million dollar aid package for an estimated 40,000 French farmers specializing in beef. The assistance includes direct support payments, funding for pre-retirement and job switches, and support aimed at strengthening beef herd production.⁽³⁹⁾

e. New Zealand

New Zealand is the third largest exporter of beef to the United States. Although New Zealand's exports are still subject to an annual TRQ of 213,402 metric tons per year, the

United States is by far its most important export market. Any beef shipped in excess of the TRQ limit is subject to a duty of 26.4 percent. Although beef shipments in 2001 to the United States fell behind 2000's levels, New Zealand did fill its TRQ, and is expected to do so again in 2002. Beef exports to Canada have also increased due to a relaxation of New Zealand's country-specific quota.

Last year, the SEO reported that New Zealand's support programs for agriculture products are the lowest among members of the OECD. The SEO identified no major policy changes in 2001 relating to the programs reviewed in 2001. SEO staff have again identified a number of small projects funded by the *Sustainable Farming Fund*, which was established in 2000.⁽⁴⁰⁾ Meat New Zealand remains engaged in marketing and research and development activities, and there are still indications of some government involvement in their activities.⁽⁴¹⁾ SEO staff continue to monitor a possible new export credit guarantee scheme, which was due to begin operating in March 2001.

f. Other Countries

In Asia, U.S. beef exports to China may increase as a result of higher demand for both low and high-end cuts and commitments made by China in its accession. The FAS reports that government plans for expanding domestic beef production focus on anticipated increases in domestic demand rather than a strategy to expand China's small export market.⁽⁴²⁾ U.S. exports to Japan were likely to decline in 2001 due to currency levels and weak domestic demand. Demand fell further when the Japanese government reported its first suspected case of BSE in September 2001. There is no indication that any of the Japanese aid programs identified in last year's report were reduced or repealed in 2001. The Republic of Korea liberalized its cattle and beef markets in January and repealed its discriminatory dual retail system for imported beef in September. U.S. exports, although lower in 2001, are expected to improve in 2002. The OECD reported several Korean domestic support programs not previously identified by the SEO, including a Calf Breeding Stabilisation Scheme, which provides a maximum deficiency payment of \$221 per calf.⁽⁴³⁾ In addition, the Korean government announced a new multi-year \$1.8 billion program to support the cattle industry.⁽⁴⁴⁾

g. Conclusion

As part of our normal ongoing work, the SEO intends to keep abreast of changing cattle and beef subsidy policies and import levels in 2002. SEO staff will also work to ensure that both U.S. industry and U.S. government officials involved in trade negotiations are kept apprised of major developments regarding the subsidy practices of these countries. One particular area where we intend to deepen our monitoring and analysis will be with respect to programs and practices affecting production in and exports from China, Japan and Korea. Given the development of technical expertise and improved regional understanding made possible by the

establishment of our Trade Remedy Compliance Staff and the deployment of Import Administration compliance officers to several posts in East Asia, we believe our ability to focus on this part of the world will be substantially strengthened in the coming year.

3. Subsidies Provided to Fertilizer Produced in India

Over the past year, USTR, the SEO and U.S. embassy personnel have been working closely with U.S. exporters of diammonium phosphate (DAP), a fertilizer product, to address Indian government fertilizer subsidies. These subsidies provide benefits to Indian producers of DAP that the U.S. industry believes adversely affect their ability to export to the Indian market. US embassy personnel in India first raised this issue with the Indian Ministries of Fertilizer, Finance and Commerce. During a USTR trip to India to discuss bilateral trade issues, the DAP subsidy program was raised as a priority problem with the Government of India (GOI).

With no resolution of this issue, USTR and the SEO deepened their involvement and have developed an ongoing dialog with the U.S. industry in its efforts to examine all possible avenues available to address this continuing problem. SEO and USTR personnel recently held informal bilateral consultations with GOI representatives in Geneva, coinciding with the WTO Subsidies Committee Meeting in October, 2001. Serious concerns were expressed to the Indian delegation, and ways were explored to further discuss and resolve this issue on a bilateral basis. Our enforcement efforts to date have been aimed at securing a quick and practical solution that avoids resorting to formal WTO dispute settlement. Absent resolution of this issue, however, we will continue to provide advice to the U.S. industry and to examine closely the DAP subsidy program and the adverse effects it may be causing.

4. Subsidies and Other Government Support to Paper Production in Germany and Korea

SEO staff have recently initiated discussions with the American Forest & Paper Association (AF&PA) to explore their concerns about the damaging effects of subsidies to expand capacity in the paper industry in Europe. The AF&PA, on behalf of its members, recently took advantage of the opportunity to provide comments to the European Commission on proposed German government subsidies for the construction of a linerboard mill in the eastern German state of Brandenburg. As a capacity-sensitive industry, the AF&PA's members expressed their opposition to these subsidies and the adverse effect they may have on competition in the corrugated base paper market within Europe but also from abroad. We plan to expand our dialog with the AF&PA and advise the industry of potential avenues to pursue this issue.

AF&PA and its member companies have also provided Commerce and USTR with a wide range of information and analysis concerning government targeting and financial assistance to Korean coated paper producers. A significant portion of the coated paper output from these mills is exported to the United States and other markets, and AF&PA believes that the Korean government's assistance has affected such international competition. Among the specific kinds

of assistance that AF&PA has identified are: low-cost facility investment loans and loan guarantees; tax benefits for facility expansion; government sponsored creation of a paper manufacturing complex; and government sale of debt obligation. We plan to evaluate and follow up on this information, in particular to assess its relationship to Korea's multilateral subsidy obligations, and will be working with the industry to determine how best to pursue the issue.

G. U.S. Enforcement and Advocacy Efforts

The United States pursues enforcement of U.S. rights under the Subsidies Agreement through WTO dispute settlement proceedings, bilateral contacts and other actions. Although any decision to initiate a dispute settlement proceeding must carefully take account of the balance of U.S. interests, our general and overarching policy objectives remain aimed at discouraging distortive subsidization and preventing or remedying harm caused to U.S. producers and workers by such subsidies. These objectives are expressed clearly in the URAA, and they provide the context in which potential subsidy enforcement complaints have been, and will continue to be, considered. USTR and Commerce work closely with one another and with the full range of federal agencies – such as the Departments of State, Treasury and Agriculture – in fulfilling this mission. This interagency cooperation is also crucial to the success of our efforts to protect and defend U.S. interests in other circumstances involving subsidy rules, such as in the explanation and defense of U.S. measures targeted by others in WTO dispute settlement and in the assistance we provide to U.S. exporters and respondent agencies subject to foreign CVD actions. In the following section, we summarize some of the principal subsidy-related disputes and activities in which the United States has been involved over the past year. [\(45\)](#)

1. Addressing Foreign Subsidies Affecting U.S. Interests

a. Korea: Direct and Indirect Government Support for Semiconductor Production and Export

Throughout 2001, USTR and Commerce worked closely with other federal agencies, in particular the Departments of State and the Treasury, and with U.S. industry to gather and analyze information and express concerns about instances of possible Korean subsidization of semiconductor production and export which could adversely affect U.S. trade interests. As we noted in last year's report, very early in 2001, representatives of the U.S. semiconductor industry brought to the attention of Commerce and USTR the fact that the government-owned Korea Development Bank (KDB) intended to purchase bonds equivalent of up to 80 percent of maturing corporate bonds issued by the heavily indebted Hyundai Electronics, Ltd. (now, Hynix Semiconductor, Inc.), among other companies. Hynix is Korea's second-largest and the world's third-largest semiconductor manufacturer. Partly as a result of past Korean government intervention and policies, Hynix has continued to grapple with untenable financial

circumstances in that an enormous concentration of its debt was coming due at a time of contracting demand for its products. As a result, both Korean government authorities and Hynix's state-owned and/or state-influenced creditor banks have taken a number of steps over the past year to keep Hynix afloat during the economic downturn.

In addition to the special one-year bond obligation which the KDB issued last January in order to help Hynix meet its "short-term" financing needs, various Korean state-owned or state-invested creditors of Hynix have over the course of the year organized several bail-out packages – involving debt roll-over, partial debt forgiveness, interest rate reductions, new lending and other forms of assistance – that have been designed to provide Hynix time and financial opportunity to restructure and wait out the market downturn. In some instances, these interventions have also provided sufficient comfort to (or placed sufficient pressure on) other creditors to offer Hynix still more flexibility in meeting its crushing debt obligations. To the extent that these steps involve government-directed or -engineered financial interventions that would not otherwise be undertaken by parties operating according to normal commercial considerations, they have implications for multilateral subsidy disciplines and Korea's obligations under those disciplines.

As noted earlier in this report, at the two regular meetings of the WTO Subsidies Committee last year, the United States formally voiced its concerns about the appropriateness of the actions of the Korean government and its affiliated banks to support Hynix. At the second meeting, U.S. objections were in large part echoed by the European Union, while Japan and Singapore also expressed interest and concern regarding the situation. In these settings and in various bilateral contacts, U.S. officials have drawn Korea's attention to its obligations under the Subsidies Agreement not to cause adverse effects to other WTO Members through the use of any subsidy, and have pointed out the questionable consistency of these interventions with the spirit of Korea's financial and market reform commitments. Both Ambassador Zoellick and Secretary Evans have raised this issue in meetings with officials at the highest levels of the Korean government, and Secretary Evans has written to his Korean counterpart urging that the government refrain from inappropriate intervention in the Hynix matter. U.S. semiconductor manufacturer, Micron, has urged that we consider challenging Korea's actions in WTO dispute settlement as being in violation of WTO subsidy rules – an option which remains under review. However, by year's end, Micron had also entered into talks with Hynix to explore the possibilities of a merger or buy-out arrangement that might have the effect of rationalizing the two firms' chipmaking operations. As of this writing, these lines of contact remain open, although the situation remains unresolved. We will continue to watch the situation closely and, if necessary, will seek enforcement of U.S. rights in the WTO, should such action be warranted.

b. Canada: Export Subsidies and Tariff-Rate Quotas on Dairy Products

In early 1998, the United States, later joined by New Zealand, commenced a WTO dispute settlement proceeding involving subsidized exports of dairy products by Canada. That

proceeding culminated in the October 1999 adoption by the WTO's Dispute Settlement Body (DSB) of the recommendations made in the Appellate Body and panel reports. Those reports found that Canada's two-tier pricing system for milk constituted an export subsidy under the provisions of the Agreement on Agriculture and that Canada had during 1997 and 1998 exported more subsidized dairy products than was permitted by its commitments under the Agriculture Agreement. The legal reasoning in those reports confirmed that governments cannot avoid their export subsidy commitments under the Agreement on Agriculture by entrusting authority to quasi-government entities. Along the lines of the definition of a subsidy described in Article 1.1(a)(1)(iv) of the Subsidies Agreement, the panel concluded that when governments delegate powers to such entities and such bodies perform governmental functions, their actions are no less governmental than had the government undertaken the acts.

In December 1999, the United States, Canada and New Zealand concluded an agreement establishing the time frame within which Canada would implement the DSB recommendations and bring its export subsidy programs into compliance with its obligations under the Agreement on Agriculture. Pursuant to that agreement, Canada changed several parts of its dairy program, including the elimination of one category of export subsidies – those which provided for the subsidized export of products made from surplus milk. However, individual Canadian provinces, working with the federal government, introduced substitute programs which, in the view of the United States, also are export subsidies and will have the same distorting effect on trade as did the previous programs.

In February 2001, the United States and New Zealand requested review of the new Canadian programs pursuant to Article 21.5 of the Dispute Settlement Understanding. At the same time, the United States and New Zealand requested authorization to withdraw concessions pursuant to Article 22 of the Dispute Settlement Understanding. Consideration of that request, however, was suspended pending completion of the Article 21.5 compliance review.

In July 2001, the Article 21.5 panel released its report in which it found that the continued involvement of Canadian federal and provincial governments in the provision of low-cost milk to processors for export constituted an export subsidy and that Canada had already exceeded its commitment under the WTO Agriculture Agreement on subsidized cheese exports. Thereafter, Canada appealed the panel report.

In October 2001, the WTO Appellate Body issued its report in which it disagreed with the panel on certain legal points but found that it was unable to reach a decision on the legality of the dairy export program due to an incomplete factual record. In response, the United States and New Zealand filed a second request pursuant to Article 21.5 for another panel hearing in order to present additional factual information. The second Article 21.5 panel report is expected to be released in July 2002.

c. European Union Support for Development of the Airbus A380 Aircraft

In January 2001, the United States and the European Union held consultations concerning the potential provision of EU government financial assistance for the Airbus A380 jetliner project and other issues regarding trade in large civil aircraft. In April 2001, the European Commission provided notification that seven Member States had made commitments to provide government loans for part of the development costs for the Airbus A380 aircraft. The United States reviewed the data provided by the EU and requested supplemental information regarding the terms and conditions of such financing to ensure that it would be consistent with the EU's obligations under the 1992 U.S.-EU Agreement Concerning the Application of the WTO Agreement on Trade in Civil Aircraft and the Subsidies Agreement. In January 2002, the EU and the United States held another round of aircraft consultations during which additional details on support for the A380 were sought. This issue will be closely monitored in the coming year.

2. Non-U.S. WTO Disputes with Systemic Importance

Canada & Brazil: Export Financing for and Measures Affecting the Export of Civil Aircraft

In 1996, Canada filed a WTO subsidies case against Brazil on behalf of its regional aircraft producer, Bombardier. The primary subsidy at issue in the case was the Programa de Financiamento às Exportações (PROEX), an interest rate "buy down" that Brazil uses to reduce the cost of financing the purchase of aircraft produced by its regional aircraft producer, Embraer. Later, in 1997, Brazil brought a separate dispute against certain alleged subsidies granted by the Canadian federal government and its provinces that support the export of aircraft produced by Bombardier.

In 1998, both of these disputes were referred to WTO panels. The panels issued final reports in March 1999, and the WTO Appellate Body issued decisions in both cases in August 1999. Each side then contested the adequacy of the other side's implementation of the panels' decisions and asked for further WTO review. The WTO ultimately concluded that Brazil had not fully withdrawn the export subsidies at issue in its case, and therefore had not fully implemented the panel's decision. It rejected Brazil's challenge to Canada's implementation.

After the WTO's decision, Brazil further modified the PROEX program, and Canada again requested a panel to review the adequacy of the modification. The panel circulated its decision in July 2001, concluding that the further modified PROEX program was not inconsistent "as such" with the SCM Agreement. There has been no further activity in the case since the panel issued its decision.

While the case was progressing, however, Canada announced that it would respond in part to Brazil's refusal to withdraw the PROEX subsidies by offering financing for a new Bombardier deal involving a U.S. carrier. Brazil responded by initiating a new panel proceeding to review

the Canadian government's action. Brazil is claiming that the export financing at issue constitutes prohibited export subsidies. Canada counters that some of the financing does not constitute a subsidy at all, and that other financing was provided to "match" Brazil's offer of WTO-inconsistent financing, and that such matching is permitted by the WTO Subsidies Agreement. The United States intervened in the case as a third party, backing Canada's argument about "matching" transactions, and backing Brazil's argument that the so-called "market window" operations of Canada's Export Development Corporation constitute export subsidies. The report of the Panel was scheduled to be released to the public in late January, 2002.

3. Defending U.S. Interests in WTO Disputes Brought by Others

a. Foreign Sales Corporation Tax Rules

In November 1997, the EU requested consultations with the United States with respect to the Foreign Sales Corporation (FSC) provisions of U.S. tax law (sections 921-927 of the Internal Revenue Code), claiming that these rules constituted a subsidy inconsistent with U.S. obligations under both the WTO Subsidies and Agriculture Agreements. The FSC provisions provide exporters with a partial tax exemption on certain foreign income of "foreign sales corporations," which are foreign subsidiaries of U.S. companies. Following consultations, a dispute settlement panel was formed and issued its report on October 8, 1999, finding that the tax exemption conferred by the FSC provisions constitutes a prohibited export subsidy under the WTO Subsidies Agreement. The panel also found that the tax exemption constitutes an export subsidy under the Agriculture Agreement, thereby resulting in a violation of U.S. obligations under that Agreement. With respect to the panel's findings under the Subsidies Agreement, the panel recommended that the United States withdraw the FSC tax exemption "with effect from" October 1, 2000.

On November 26, 1999, the United States appealed the panel's findings, and, subsequently, the EU also appealed the panel's resolution of certain issues. The Appellate Body circulated its report on February 24, 2000. The Appellate Body upheld the panel's finding that the FSC tax exemption constitutes a prohibited export subsidy under the SCM Agreement, although its reasoning differed somewhat from that of the panel. The Appellate Body reversed the panel's finding that the FSC tax exemption fell under Article 9.1(d) of the Agriculture Agreement. However, the Appellate Body found that the FSC tax exemption nonetheless was an "export subsidy" within the meaning of Article 1(e) of the Agriculture Agreement which resulted in, or which threatened to lead to, circumvention of U.S. export subsidy commitments with respect to both scheduled and unscheduled agricultural products.

The DSB adopted the panel and Appellate Body reports on March 20, 2000. On April 7, the United States informed the DSB of its intention to implement the recommendations and rulings in a manner which respects U.S. WTO obligations. Throughout the spring and

summer, the Executive Branch worked with Congress and the private sector to develop legislation which would: (1) repeal the FSC provisions; and (2) provide tax treatment for foreign sales similar to that afforded by territorial-type tax regimes, such as are found in Europe. The United States consulted with the EU as the legislation was being developed, and the EU made known that it would challenge the WTO-consistency of the legislation being developed. As a result, in order to avoid further escalation of bilateral tensions, the United States and the EU agreed on September 29 on procedures to govern any EU challenge to the FSC replacement legislation. The agreement essentially provides that the WTO-consistency of the replacement legislation be resolved before considering questions relating to what, if any, countermeasures might be imposed by the EU.

After it became apparent that the United States would be unable to meet the October 1 deadline, the United States requested, and the DSB agreed, to extend the deadline to November 1, 2000. On November 15, the United States enacted the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (the ETI Act). The ETI Act repeals the FSC provisions and establishes a new regime under which extraterritorial income – as defined in the Act – is not subject to tax.

On November 17, under Article 21.5 of the DSU and in accordance with the U.S./EU procedural agreement, the EU requested dispute settlement consultations with respect to the Act. On the same day, and also in accordance with the procedural agreement, the EU requested authority from the DSB to take countermeasures and suspend concessions in the amount of \$4.043 billion per year. On November 27, the United States objected to the appropriateness of the countermeasures and the level of suspensions proposed by the EU, thereby resulting in the referral of the matter to arbitration.

Following consultations, the EU on December 7 requested the establishment of a dispute settlement panel to review the compatibility of the Act with WTO obligations. On December 20, the DSB established a panel under Article 21.5 of the DSU to consider the EU's claims regarding the WTO-consistency of the Act. The panel is composed of the three panelists from the original proceeding. On December 21, the United States and the EU, in accordance with the procedural agreement, jointly requested that the arbitrators (also the three original panelists) suspend the arbitration proceedings until the adoption of the panel report or, in the event of an appeal, the Appellate Body report in the Article 21.5 proceeding.

The panel circulated its final report on August 20, 2001. The panel found the ETI Act to be inconsistent with U.S. obligations under the WTO in the following respects: (1) the panel found that the ETI Act's tax exclusion constitutes an export subsidy that is prohibited by the SCM Agreement and that is inconsistent with U.S. export subsidy commitments under the Agriculture Agreement; (2) the ETI Act's 50 percent foreign value rule is inconsistent with Article III:4 of GATT 1994; and (3) the ETI Act's transition rules are inconsistent with the DSB's recommendation to withdraw the FSC subsidy with effect from November 1, 2000.

On October 15, the United States appealed the panel's findings, and, subsequently, the EU also appealed the panel's resolution of certain issues. On January 14, 2002, the Appellate Body affirmed the findings of the panel. The Administration is studying this decision carefully and will consult closely with Congress to resolve this dispute.

b. *Canada's Challenge of CVD Law's Treatment of Export Restraints as Potential Subsidies*

On May 19, 2000, Canada requested consultations with the United States regarding U.S. measures that treat a government-directed or -imposed restraint on exports of a product as a potential subsidy to other products made using or incorporating the restricted product if the domestic price of the restricted product is affected by the restraint. The specific measures identified by Canada were: (1) portions of the Statement of Administrative Action (SAA) accompanying the URAA; and (2) portions of the preamble to Commerce's 1998 notice of final rulemaking promulgating substantive CVD regulations. Consultations were held on June 15, 2000. On July 24, Canada requested that the DSB establish a panel. In its panel request, Canada identified the measures as: (1) section 771(5) of the Tariff Act of 1930, as amended, as interpreted by the SAA and the preamble; and (2) U.S. practice thereunder. (Section 771(5) defines the term "subsidy" for purposes of the U.S. countervailing duty law.) The DSB established a panel at its meeting on September 11, and Australia, the EU and India reserved their rights as third parties.

From the standpoint of CVD methodology, the key issue in this dispute was whether, as alleged by Canada, an export restraint can never, under any set of circumstances, constitute a "financial contribution," one of the prerequisite elements of a subsidy. In its submissions to the panel, the United States took the position that, based upon the application of standard rules of treaty interpretation, Canada's allegation was unfounded.

An even more important issue in the dispute, however, was a jurisprudential one. None of the so-called "measures" cited by Canada mandated that Commerce treat an export restraint as a financial contribution. Therefore, even if the panel agreed with Canada's assertions regarding the status of export restraints, based upon the traditional GATT/WTO distinction between mandatory and discretionary measures, the panel had to find that none of these "measures" was inconsistent with U.S. WTO obligations. The United States argued that, under these circumstances, what Canada actually was asking the panel to do was to issue an advisory opinion regarding the status of export restraints under the Subsidies Agreement. On December 12, 2000, the United States filed a request for preliminary findings by the panel which, had it been granted, would have resulted in the early dismissal of Canada's complaint.

The panel did not make preliminary findings, but instead considered the U.S. arguments in the context of its final report, which it circulated on June 29, 2001. The panel agreed with the United States that none of the "measures" required Commerce to treat export restraints as financial contributions. Therefore, based upon the mandatory/discretionary doctrine, none of

the "measures" was inconsistent with U.S. WTO obligations.

In one portion of the report, the panel did opine that an export restraint, as defined by Canada for purposes of the dispute, cannot constitute a financial contribution within the meaning of Article 1 of the Subsidies Agreement. In addition to being dicta, this portion of the report is very narrow dicta. The panel stated that it was not opining on the status of other measures that might fall under the label of "export restraints."

Neither the United States nor Canada appealed the panel report. As a result, the report was adopted on August 23, 2001, and no further action was required by the United States.

c. "Privatization" or "Change-in-Ownership" CVD Methodology Disputes

On June 30, 1998, the EU requested consultations with the United States with regard to the imposition of countervailing duties on certain hot-rolled lead and bismuth carbon steel (lead bar) from the United Kingdom (UK). The EU contended that Commerce had inappropriately imposed countervailing duties on two private successor companies to government-owned British Steel Corporation (BSC) based on a methodology that incorrectly attributed a portion of the massive subsidies originally received by BSC prior to its privatization in 1988 to the two successor companies. Following consultations held in July, a panel was established.

At the center of this dispute was the approach taken under Commerce's methodology for handling certain "pre-privatization" subsidies. In its report, the panel found that Commerce had imposed countervailing duties on U.S. imports from the two privatized companies in violation of the Subsidies Agreement. In reaching its decision, the panel disagreed with how Commerce accounts for the privatization of a government-owned company and determined that an investigating authority (such as Commerce) had to reassess whether pre-privatization subsidy benefits continue to exist after a company is sold to new owners.

The panel also clarified the applicable standard of review. It found inapplicable the standard of review expressly set forth in the WTO Antidumping Agreement, which provides that dispute resolution panels should uphold permissible interpretations of that agreement by national administering authorities, even if the panels themselves would have reached different conclusions.

On January 27, 2000, the United States notified the DSB that it would appeal the panel's decision.

The Appellate Body circulated its report on May 10, 2000, upholding the panel finding, although its reasoning was somewhat different. In particular, the Appellate Body emphasized that an investigating authority could presume the continuation of a subsidy benefit over a period of years. However, it agreed with the panel's holding that if the company under

investigation was a different "legal person" from the original subsidy recipient, an analysis of the privatization transaction had to be undertaken to determine whether a subsidy benefit could be attributed to the privatized company. The Appellate Body also stated that its findings were limited to the particular circumstances of the case before it.

While the panel and Appellate Body proceedings were pending, Commerce was conducting a "sunset review" of the CVD order on UK lead bar. In the course of that review, the U.S. petitioners expressed no interest in maintaining the order, and requested that the order be revoked with retroactive effect so as to cover the administrative reviews that were the subject of the WTO dispute. As a result, by the time the Appellate Body issued its report, Commerce already had revoked the order and canceled the imposition of any countervailing duties on imports covered by the contested administrative reviews. Accordingly, at the DSB meeting on July 5, 2000, the United States stated that no further action was necessary to implement the recommendations of the DSB.

While the WTO dispute was ongoing, there was a significant domestic legal development. On February 2, 2000, the Court of Appeals for the Federal Circuit (CAFC) found Commerce's privatization or "change of ownership" methodology to be inconsistent with U.S. law. This case – *Delverde, SRL v. United States*, 202 F.3d 1360 – involved a transaction between two private firms, but the methodology employed by Commerce was essentially the same as the methodology it used to examine the privatization of government-owned firms. In the meantime, the CAFC denied Commerce's request for a rehearing by the entire court, and the Administration declined to seek further review by the U.S. Supreme Court. Accordingly, Commerce began the process of reexamining its privatization and change of ownership methodologies in light of the *Delverde* decision. As part of this process, Commerce requested remands from the Court of International Trade (CIT) in those cases where these methodologies were at issue in order to allow Commerce to make revised determinations consistent with the CAFC's decision.

On November 10, 2000, the EU requested dispute settlement consultations with respect to 14 outstanding U.S. CVD orders involving imports from various EU member states in which there was a change-in-ownership issue. Consultations were held on December 7.

On December 21, 2000, Brazil also requested dispute settlement consultations with respect to Commerce's privatization methodology. The two U.S. CVD measures cited in the consultation request were a sunset review determination in cut-to-length plate from Brazil and the suspended final determination in certain hot-rolled steel from Brazil. Consultations were held in Geneva on January 17, 2001.

Shortly after the EU consultation request, however, Commerce issued draft redeterminations in four of the cases in which it had obtained remands from the CIT. In these redeterminations, Commerce applied a revised methodology under which it examined, first, whether the

producer/exporter of the subject merchandise was the same person that had received a subsidy prior to privatization or a change in ownership. In these four cases, based upon a review of the record evidence, Commerce determined that the entity was the same and, accordingly, determined that the benefit from the original subsidies continued. If Commerce had found the pre-sale and post-sale entities to be different legal persons, it would have then analyzed the privatization transaction to determine whether a subsidy had been provided to the post-sale entity.

The EU requested a further round of consultations to consider, among other things, Commerce's revised methodology. Consultations were held in Geneva on April 3, 2001.

On August 8, 2001, the EU requested the establishment of a dispute settlement panel with respect to 12 of the 14 CVD proceedings identified in its original consultation request. The EU is challenging Commerce's revised methodology, as well as what the EU perceives to be the continued application by Commerce of its former methodology. The DSB established a panel on September 10, with Brazil, India and Mexico reserving their right to participate as third parties.

The EU filed its first written submission to the panel on December 21. The first U.S. written submission was filed on January 23, 2002. The first meeting with the panel is scheduled for February 19-21, 2002.

However, as in the first panel proceeding involving UK lead bar, there has been a significant domestic legal development. On January 4, 2002, the CIT issued two decisions in which it held that Commerce's revised change of ownership methodology was inconsistent with the U. S. CVD statute, as interpreted by the CAFC in *Delverde*. The CIT remanded the agency determinations in question – both of which are the subject of the pending panel proceeding – to Commerce for redeterminations consistent with the court's opinion. The two CIT decisions are *Allegheny Ludlum Corp. v. United States*, Slip Op. 02-01, and *GTS Industries S.A. v. United States*, Slip Op. 02-02.

d. EU's Challenge of CVD Review of Certain Corrosion-Resistant Carbon Steel Flat Products from Germany

On November 10, 2000, simultaneous with its request regarding the 14 CVD orders where privatization or change in ownership is at issue, the EU also requested dispute settlement consultations with the United States with respect to the imposition of countervailing duties on certain corrosion-resistant carbon steel flat products from Germany. Consultations were held in Geneva on December 8, 2000.

Initially, the crux of the EU complaint appeared to be that the United States does not apply the one percent de minimis subsidy standard of Article 11.9 of the Subsidies Agreement to the

sunset review phase of CVD proceedings, but instead, by regulation, applies a de minimis standard of 0.5 percent. The U.S. position is that Article 11.9, by its terms, is limited to the investigation phase of a CVD proceeding and that the Subsidies Agreement does not impose any de minimis standard for the sunset review phase.

On February 5, 2001, the EU filed a second request for consultations. In this second request, the EU expanded its complaint to include allegations regarding certain basic aspects of U.S. procedures for sunset reviews, including the U.S. statutory requirement that Commerce self-initiate sunset reviews in all cases. Consultations were held in Geneva on March 21, 2001.

On August 8, the EU requested the establishment of a dispute settlement panel. The DSB established a panel on September 10, with Japan and Norway reserving their rights to participate as third parties. The EU filed its first written submission to the panel on December 13. The first U.S. written submission was filed on January 15, 2002. Japan and Norway filed their first submissions on January 22. The first meeting with the panel was held on January 29-30. Second written submissions are due on February 21 and the second meeting of the panel is scheduled to be held on March 19, 2002.

e. Canada's Challenge to Section 129(c)(1) of the Uruguay Round Agreements Act

Section 129(c)(1) of the URAA (19 U.S.C. § 3538(c)(1)) is a provision of U.S. law that addresses the treatment of unliquidated entries of subject merchandise in situations where the United States responds to a WTO panel decision by revoking a U.S. AD or CVD order or otherwise modifying an AD or CVD determination. On January 17, 2001, Canada requested consultations with the United States with respect to Section 129(c)(1), claiming that the provision is inconsistent with U.S. obligations under the Dispute Settlement Understanding (DSU), GATT 1994 and the Subsidies and Antidumping Agreements. The United States and Canada held consultations on the matter but were unable to resolve their differences. On July 12, 2001, Canada requested that a panel be established. The panel was established on August 23, 2001 and constituted on October 30, 2001.

On December 19, 2001, Canada filed its first written submission in the case. Canada continues to argue that Section 129(c)(1) is inconsistent with the GATT and the Subsidies and Antidumping Agreements. However, Canada did not claim in its submission that Section 129(c)(1) is inconsistent with any provisions of the DSU.

The United States filed its first written submission on January 29, 2002. The United States believes that Canada's claims are not well-founded for various reasons, including that Canada's interpretation of the interaction between section 129(c)(1) and the WTO provisions at issue would inappropriately require the United States to provide retroactive relief in AD and CVD cases. The first meeting of the panel is scheduled to take place on February 18 and 19, 2002.

f. Canada's Challenge of Preliminary Determinations with Respect to Softwood Lumber

On August 9, 2001, Commerce made an affirmative preliminary countervailing duty determination and an affirmative preliminary critical circumstances determination with respect to softwood lumber from Canada. On August 21, 2001, Canada requested WTO consultations with the United States, alleging that Commerce's determinations were inconsistent with various provisions of the Subsidies Agreement and GATT 1994.

Canada is challenging three separate aspects of Commerce's determinations. First, Canada challenges Commerce's preliminary finding that provincial "stumpage" fees (the fees for harvesting trees) confer a subsidy because Commerce determined that six provinces charge lower fees than private suppliers in comparable areas of the United States. Canada claims, among other things, that stumpage does not constitute a "financial contribution," that stumpage does not benefit a "specific" industry, and that prices charged by Canadian, rather than U.S., private suppliers are the proper benchmark for determining whether stumpage conveys a subsidy.

Second, Canada challenges Commerce's preliminary finding that "critical circumstances" exist in this case. A "critical circumstances" determination is designed to provide a remedy for injury resulting from import surges occurring before countervailing duties are imposed. If Commerce and the ITC make final affirmative determinations that critical circumstances exist, duties will be imposed retroactively on imports during the 90-day period prior to the publication of the preliminary determination. Commerce preliminarily found that critical circumstances exist in this case based on its determination that the two statutory prerequisites for such a finding were satisfied: (1) certain of the alleged subsidies were inconsistent with the Subsidies Agreement; and (2) there were massive imports from Canada over a relatively short period of time. Canada challenges this determination, claiming, among other things, that the rate for the inconsistent subsidy is de minimis and that Commerce's determination improperly purports to apply retroactive duties based, in part, on other subsidies that are not inconsistent with the SCM Agreement.

Third, Canada challenges Commerce's preliminary calculation of an aggregate countervailing duty rate, applicable to all producers and exporters, rather than company-specific rates, because of the extraordinarily large number of Canadian producers. More specifically, Canada challenges certain U.S. statutory and regulatory provisions on the ground that they improperly fail to provide for company-specific expedited or administrative reviews in cases in which the investigation was conducted on an aggregate basis.

Following U.S.-Canadian consultations in September, the DSB established a panel on December 5, 2001. On December 17, 2001, Japan notified the DSB that it plans to participate in the panel proceedings as a third party. The EU and India have also reserved their third-party rights.

3. Defending Interests of the United States in Foreign Countervailing Duty Cases

Canadian Countervailing Duty Investigation of Grain Corn from the United States

On June 19, 2000, the Manitoba Corn Growers' Association filed a countervailing duty complaint with the Canadian Customs and Revenue Agency (CCRA) against grain corn from the United States. The complaint alleged that over 36 U.S. federal and state programs were providing subsidies to corn producers in the United States and that exports of U.S. corn were injuring corn producers in western Canada. Although the U.S. government submitted a formal argument in opposition, the CCRA began a CVD investigation on August 9, 2000.

Throughout the CVD investigation, USTR, Commerce and the Department of Agriculture forcefully defended the interests of the U.S. corn industry. In addition to providing extensive factual information to the Canadian authorities, numerous procedural objections and substantive arguments were formally made in writing and in the course of several meetings held with the Canadian authorities.

On February 5, 2001, the CCRA issued its final determination in the investigation, finding a combined 35 percent subsidy rate from the following three programs: (1) Loan Deficiency Payments and Marketing Assistance Loans, (2) Marketing Loss Assistance Payments, and (3) the Federal Crop Insurance Program. However, on March 7, 2001, the Canadian International Trade Tribunal issued a final determination that imports of U.S. subsidized grain corn have not caused or threatened injury to the production of grain corn in western Canada. Accordingly, the investigation was terminated and all provisional duties that had been collected prior to the final determination were refunded.

CONCLUSION

In the coming year, USTR and Commerce will continue the vigorous enforcement of the rules and disciplines of the WTO Subsidies Agreement and take strong, pro-active steps to address the impact of distortive subsidies on American firms and their workers in both the United States and foreign markets. To accomplish this, the Administration, working together with Congress, will assertively put forward its affirmative agenda in the forthcoming WTO rules negotiations, in order to effectuate our objective of strengthening the international subsidy discipline regime and address the subsidy concerns in key sectors of the U.S. economy.

The past year marks an important turning point in the marshaling of government resources to deal with distortive foreign subsidies. The new, Administration-wide trade compliance initiative launched in 2001 will increase our monitoring and enforcement capabilities. Nowhere is this more critical than with respect to China, whose accession to the WTO opens the door to increased and more predictable trading opportunities, but also presents the

challenge of ensuring that China adheres faithfully to the critical commitments it has made to trade fairly.

As we move forward throughout the upcoming year, we will continue to work with the Congress as we pursue a pro-active agenda to safeguard the interests of U.S. industries and workers facing unfairly subsidized foreign competition.

ATTACHMENT 1

TRADE REMEDY COMPLIANCE STAFF *PRO-ACTIVELY ADDRESSING UNFAIR TRADE PROBLEMS*

The Trade Remedy Compliance Staff

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

TRCS Activities

Washington, D.C.

- Monitor data on imports into the United States, as well as foreign government policies and economic/business trends that may contribute to unfair trade problems.
- Analyze other countries' development and use of their AD, CVD and other trade remedy statutes.
- Provide information related to the enforcement of U.S. AD/CVD laws to foreign and domestic parties.

Overseas

- Interact with foreign officials in matters directly related to the administration of U.S. AD/CVD laws, in support of Washington-based case analysts.
- Collect, assess, and confirm information about certain foreign market conditions, trade practices, and governmental policies that would facilitate administration of U.S. unfair trade laws or U.S. monitoring of unfair trade commitments.

The TRCS Role and Service

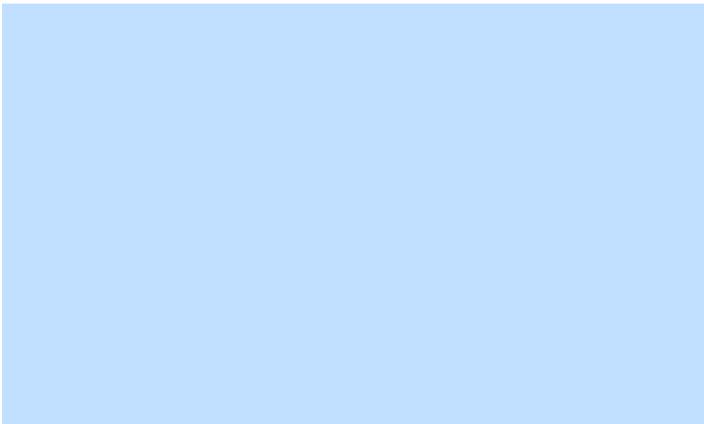
IA's central role remains the enforcement of the U.S. antidumping (AD) and countervailing duty (CVD) laws. However, IA has built upon its law enforcement duties by instituting a variety of import monitoring and subsidies enforcement activities designed to help American industry deal more effectively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

TRCS Initiatives Under Way

TRCS personnel in Washington are organized on a country-specific basis (i.e., China, Japan, Korea and Taiwan). They continually develop key information sources and data bases to study imports into the United States and evaluate the status and evolution of foreign government policies and market developments that might contribute to unfair trade. Analyses of these countries' AD, CVD and safeguards laws and actions are also performed to identify potential difficulties for U.S.

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

exporters and/or conflicts with WTO obligations or basic precepts of transparency and due process. One example of the TRCS's contributions thus far is its monitoring of China's WTO-related subsidies and unfair trade law obligations as part of the U.S. Government's broader efforts to verify Chinese compliance with WTO accession commitments.



Need further information?

Please contact:

Ron Lorentzen, Director, Trade Remedy Compliance Staff

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E-mail: Ronald_Lorentzen@ita.doc.gov

ATTACHMENT 2

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

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

Types of Subsidies: A subsidy can be almost anything a government does, if the following conditions are met: (1) a financial contribution is made by a government or public body and (2) a benefit is received by the company. Trade rules permit remedies in

As an illustration:

A U.S. exporter is bidding on a project in Country A and is competing against an exporter from Country B. The company from Country B offers a bid that is extremely low, possibly even below what one would assume to be the cost of production. The U.S. exporter may have knowledge that the reason the company from Country B is

circumstances when subsidies are "specific" (*i.e.*, provided to a limited number of companies, such as all exporters) and have caused adverse trade effects. Subsidies can take a variety of forms. Following are some of the types of foreign subsidies that could place a U.S. exporter at a competitive disadvantage vis-a-vis a foreign competitor.

o *Export financing* at preferential rates.

o *Grants or Tax exemptions* for favored companies or industries.

o *Loans that are conditioned on meeting local content requirements*, or are contingent upon the use of domestic goods over U.S. exports (commonly referred to as "import substitution subsidies").

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

Questions and information can be referred to:
Carole Showers tel.: (202) 482-3217
fax : (202) 501-7952
e-mail: Carole_Showers@ita.doc.gov

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

Working Together to Assist U.S. Exporters: The SEO welcomes any information about foreign subsidy practices that may adversely affect U.S. companies' export efforts. The SEO can

evaluate the subsidy in relation to U.S. and multilateral trade rules to determine what action may be possible to take to counteract such adverse effects. By working together to monitor foreign subsidies and enforce the Subsidies Agreement, we can ensure that U.S. companies are competing in a fair international trading system.

ATTACHMENT 3

First Screen

ELECTRONIC SUBSIDIES ENFORCEMENT LIBRARY

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

Reports to Congress

- **1998 Annual Report on Subsidies Enforcement - February 1998**
- **1999 Annual Report on Subsidies Enforcement - February 1999**
- **2000 Annual Report on Subsidies Enforcement - February 2000**
- **2001 Annual Report on Subsidies Enforcement - February 2001**
- **Review and Operation of the WTO Subsidies Agreement - June 1999**

Description of Choices

- **WTO Agreement on Subsidies and Countervailing Measures**

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

- **Overview of the Subsidies Enforcement Office**

This links the visitor to the informational page found in Attachment 1 to this Report. As shown in Attachment 1, information contained on this page includes a general overview of the SEO, and contact information for the SEO.

- **Subsidy Programs Investigated by DOC**

This links the visitor to subsidy programs which were analyzed by Import Administration staff during countervailing duty (CVD) proceedings. This section is newly redesigned and will more easily provide visitors access to the information which they are seeking. After clicking on the above choice, visitors will be linked to a page which has an alphabetical drop-down list of countries which were investigated during CVD proceedings. As of December 2000, this list

comprised 51 countries. After selecting a country to review, visitors have the option of selecting subsidy programs within that country that are not "in name" specific to a certain industrial sector ("general") and programs that are used only by certain sectors ("industry"). For example:

Argentina					
Subsidy Type	Program Codes				
General	1	2	3	4	5
Industry	1	2	3	4	5

Thus, if a visitor were interested in finding more information about subsidies to the steel sector in Argentina, he or she would click on the "Industry" link in the above table and then examine the information provided. Once a subsidy program of interest is found in this section, visitors are provided a description of the program and are able to easily view the cases in which the program was analyzed. Further information about the program in a specific case can be easily found by clicking on the hyperlinked cite to the Federal Register notice in which a complete description of the program and Commerce's analysis is provided.

The second sub-division of programs within this topic, as shown above, is based on the classification of the subsidy program by Commerce. There are five categorizations: (1) countervailable, (2) not countervailable, (3) terminated, (4) not used, and (5) found not to exist. These categories track the methodology used by Commerce and found in its decisions as published in the Federal Register. Descriptions for each of these terms are provided in the Subsidies Library. This level of detail allows a visitor to the library to find the exact type of information he or she is seeking.

Using the same example as described above, if a visitor were interested in discovering which subsidy programs Commerce had countervailed involving steel products exported from Argentina, he or she would select **Argentina » Industry » Countervailable Programs** and then review the information provided. If more detailed information about a particular subsidy program is required, a click of the mouse on the Federal Register cite next to the individual cases will take the visitor directly into the Federal Register notice where such information is readily available.

The following list shows the 51 U.S. trading partners which have had programs investigated in U.S. CVD proceedings, and information about which can be found in the Subsidies Enforcement database:

Argentina	India	Philippines
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Australia	Indonesia	Poland
Austria	Iran	Portugal
Bangladesh	Ireland	Saudi Arabia
Belgium	Israel	Singapore
Brazil	Italy	South Africa
Canada	Japan	Spain
Chile	Kenya	Sri Lanka
Colombia	Korea	Sweden
Costa Rica	Luxembourg	Taiwan
Denmark	Malaysia	Thailand
Ecuador	Mexico	Trinidad and Tobago
El Salvador	Netherlands	Turkey
European Union	New Zealand	United Kingdom
France	Norway	Uruguay
Germany	Pakistan	Venezuela
Greece	Peru	Zimbabwe

- **WTO Subsidies Notifications**

This will link the visitor to all derestricted WTO subsidy notifications, by country. Beneath each country's name is the date the document was submitted to the WTO and the date it was posted to the WTO website. This listing provides each type of notification, i.e., *new and full, update* or a *supplement to an earlier filing*. (See discussion above in this Report.) Clicking on the name of the country next to the document of interest will take the visitor directly to that country's subsidy notification. If subsidies have been notified, a listing of those subsidies is provided, in addition to specific information concerning the subsidy program, such as the type of incentive provided, the duration and purpose of the program, and the governing law or provision of the incentive. Several of the larger countries have provided information on hundreds of subsidy practices. Although the Subsidies Agreement stipulates that the notification of a subsidy practice does not prejudice its legal status under the Agreement, these notifications do provide detailed information concerning a number of countries' subsidy measures. In the event that less than full information about the program is provided, the Subsidies Enforcement Office, working with other Agencies, seeks more detailed information.

Reports to Congress

- **1998 Annual Report on Subsidies Enforcement - February 1998**
- **1998 Annual Report on Subsidies Enforcement - February 1998**
- **1999 Annual Report on Subsidies Enforcement - February 1999**
- **2000 Annual Report on Subsidies Enforcement - February 2000**
- **2001 Annual Report on Subsidies Enforcement - February 2001**
- **2002 Annual Report on Subsidies Enforcement - February 2002**

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

Reports to Congress

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

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

ENDNOTES

1. Prior to 2000, Article 8 of the Agreement provided that certain limited kinds of government assistance granted for industrial research and development (R&D), regional development, or environmental compliance purposes would also be treated as a non-actionable subsidy so long as such assistance conformed to the applicable terms and conditions for green light subsidies set forth in Article 8. In addition, Article 6.1 of the Agreement provided that certain other subsidies, referred to as dark amber subsidies, could be presumed to cause serious prejudice. These were: (i) subsidies to cover an industry's operating losses; (ii) repeated subsidies to cover a firm's operating losses; (iii) the direct forgiveness of debt (including grants for debt repayment); and (iv) when the ad valorem subsidization of a product exceeds five percent. If such subsidies were challenged on the basis of these dark amber provisions in a WTO dispute settlement proceeding, the subsidizing government would have the burden of showing that serious prejudice had not resulted from the subsidy. However, as explained in our 2000 report, a mandatory review was conducted in 1999 under Article 31 of the Agreement to determine whether to extend the application of the green light and dark amber provisions beyond December 31 of that year. Because a consensus could not be reached among WTO Members on whether or the terms by which these provisions might be extended beyond their five-year period of provisional application, they expired on January 1, 2000. ([Back](#))

2. The WTO Committee on Agriculture also devoted considerable attention to the matter of agricultural subsidies last year in the course of both its ongoing review of implementation of reduction commitments made in the Uruguay Round and its special sessions in which negotiations are under way to increase disciplines on trade-distorting domestic supports and export subsidies. [\(Back\)](#)

3. Article 24 of the Agreement directs the Committee to establish a Permanent Group of Experts (PGE), "composed of five independent persons, highly qualified in the fields of subsidies and trade relations." The Agreement articulates three possible roles for the PGE: (i) to provide, at the request of a dispute settlement panel, a binding ruling on whether a particular practice brought before that panel constitutes a prohibited subsidy, within the meaning of Article 3 of the Agreement; (ii) to provide, at the request of the Committee, an advisory opinion on the existence and nature of any subsidy; and (iii) to provide, at the request of a WTO Member, a "confidential" advisory opinion on the nature of any subsidy proposed to be introduced or currently maintained by that Member. (To date, the PGE has not yet been called upon to perform any of the aforementioned duties.) Article 24 further provides for the Committee to elect the experts to the PGE, with one of the five experts being replaced every year. One PGE member, Mr. A. V. Ganesan of India, resigned his membership, effective May 18, 2000, prior to the end of his term. At a special meeting in February 2001, the Committee elected Professor Okan Aktan (Turkey) to replace Mr. Ganesan, for the remainder of Mr. Ganesan's term, which expires in 2002. At its May 2001 regular meeting, the Committee elected Mr. Jorge Castro Bernieri (Venezuela) to replace Mr. Horlick (United States), whose term expired in 2001. Other Members of the PGE include Mr. Marco Bronckers (Netherlands), Professor R.G. Flores Junior (Brazil), and Mr. Hyung-Jin Kim (Korea). [\(Back\)](#)

4. As of this writing, the United States is continuing its efforts to finalize a consolidated updating notification for 1999 and 2000, and a new and full notification for 2001. Beyond updating information on federal programs, the need to update and expand upon more than 200 individual measures reported at the sub-federal level in our previous notification is one of the reasons for this delay. [\(Back\)](#)

5. Any extension granted by the Committee would only preclude a WTO dispute settlement case from being brought against the export subsidies at issue. This provision does not limit a Member's ability to bring a CVD action under its national laws. [\(Back\)](#)

6. El Salvador and Jamaica made the initial proposals in this area. [\(Back\)](#)

7. In addition to agreement on the specific length of the extension, it was also agreed at the Fourth Ministerial Conference, in essence, that the Committee should look favorably upon the extension requests of Members which do not meet all the specific

eligibility criteria for the special small exporter procedures but which are similar situated to those that do meet all the criteria. [\(Back\)](#)

8. Colombia, EL Salvador, Panama and Thailand have also requested an extension for their export subsidy programs under the normal Article 27.4 provisions of the Agreement [\(Back\)](#)
9. Such subsidies would nonetheless still be actionable pursuant to a CVD proceeding initiated by a Member. [\(Back\)](#)
10. This de minimis subsidy level for Annex VII countries is 3 percent, compared with the 2 percent level applicable in investigations involving other developing countries. [\(Back\)](#)
11. Annex VII(b) countries are Bolivia, Cameroon, Congo, Cote d'Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka, and Zimbabwe. In recognition of a technical error made in the initial compilation of this list and pursuant to a General Council decision, Honduras was formally added to Annex VII(b) on January 20, 2001. [\(Back\)](#)
12. While some Members were concerned that they might graduate from Annex VII due, in part, to inflation, other countries were concerned that use of constant 1990 dollars might result in their being closer to Annex VII graduation relative to their position calculated using nominal dollars. [\(Back\)](#)
13. The addition of the phrase "for three consecutive years" was added at the request of Honduras which was concerned that its possible graduation from Annex VII in the near future might place it in a worse condition than those Members which avail themselves of the special procedures under Article 27.4 for small exporter developing countries. [\(Back\)](#)
14. None of these proposal were discussed in the Subsidies Committee. [\(Back\)](#)
15. Although permissible under the Agreement when provided by a least-developed country, such export subsidies remain subject to CVD actions brought under national laws. [\(Back\)](#)
16. As regards countervailing duty rules, the Protocol of Accession makes clear that other WTO Members may apply countervailing measures to imports from China, consistent with the rules and procedures of the WTO Subsidies Agreement, but it also recognizes

that investigating authorities may be compelled to resort to alternative methods to identify and measure subsidies in circumstances where there are "special difficulties" associated with using Chinese benchmarks. ([Back](#))

17. In conducting its analysis, the ITC broke out the four categories into 33 product categories. ([Back](#))
18. Including tie votes. ([Back](#))
19. Although disagreeing over the extent of overcapacity, most industry experts considered excess inefficient capacity to be a significant problem in the global steel industry that exacerbates downturns in the market and contributes to trade distortions in the world steel market. Despite these conclusions, until the September OECD meeting, a number of major steel producing nations refused to acknowledge that excess inefficient capacity presented a problem for the global steel industry. ([Back](#))
20. As explained earlier, in order for subsidies to be actionable, other than prohibited subsidies, they must be specific (e.g., provided to a single firm or industry or a group thereof) and cause adverse effects to the interests of another Member. Adverse trade effects can include (1) material injury to the domestic industry, or the threat thereof, as in CVD proceedings, (2) the nullification or impairment of benefits accruing directly or indirectly to another WTO Member under the GATT 1994, and (3) the displacement or impeding of sales or significant price undercutting, price suppression or price depression in so-called "serious prejudice" disputes brought to the WTO. Because serious prejudice can arise in any market affected by an actionable subsidy (whether in an importing country, the subsidizing country, or a third-country market), it is the standard most often used to challenge subsidized competition in the subsidizing country or third-country markets. ([Back](#))
21. The Advocacy Center helps U.S. exporters seek contracts abroad on an equal footing with foreign government-backed competitors. ([Back](#))
22. Foreign service nationals are professional employees of U.S. embassies and consulates who are natives of the country in which the embassies are located. These employees assist foreign service and USCS officers with their assigned duties. ([Back](#))
23. CLDP is a Commerce initiative funded in part by the U.S. Agency for International Development. It is one component of the U.S. Government effort to support economic and political reforms underway around the globe. ([Back](#))
24. An important factor in a U.S. company's ability to do business in any given market is

the manner in which the foreign government administers its unfair trade laws and, in particular, its CVD and AD laws. Import Administration monitors these foreign AD and CVD actions involving U.S. companies to ensure that the foreign governments are conducting these investigations in accordance with their international obligations.

[\(Back\)](#)

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39. "France Livestock and Products, New Subsidy for French Beef Farmers, Global Agricultural Information Network Report #FR2002," United States Department of Agriculture, Foreign Agricultural Service, January 11, 2002. ([Back](#))
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45. Information about WTO dispute settlement proceedings is available to the public on the World Wide Web at: http://www.wto.org/wto/english/tratop_e/dispu_e/distab_e.htm. ([Back](#))

