

**SUBSIDIES ENFORCEMENT
ANNUAL REPORT TO THE CONGRESS**

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

This report describes the efforts by the Office of the U.S. Trade Representative (USTR) and the U.S. Department of Commerce (Commerce), in close cooperation with other Executive Branch agencies, to monitor and challenge unfair foreign government subsidy practices in 2009. Section 281(f)(4) of the Uruguay Round Agreements Act mandates that USTR and Commerce submit a joint report to the Congress each year that describes the Administration's subsidy monitoring and enforcement activities throughout the previous year. This report is the fifteenth annual report submitted to the Congress.

In 2009, American workers and industries continued to face unfavorable economic conditions. In response to the sharp economic downturn in 2008 and at the beginning of 2009, many governments worldwide, including the United States, introduced or announced measures to address new challenges arising from the economic crisis. The United States remains committed to ensuring that all Members of the World Trade Organization (WTO), when adopting such measures, adhere to their obligations under the applicable agreements and, when measures distort trade and adversely affect U.S. interests, the United States will exercise its rights as necessary under those agreements.

The principal tool available to WTO Members to remedy harmful subsidy practices worldwide is the WTO Agreement on Subsidies and Countervailing Measures (Subsidies Agreement), which establishes multilateral disciplines on subsidies. In the WTO, the Committee on Subsidies and Countervailing Measures (Subsidies Committee) serves as the primary forum for WTO Members' subsidy-related work and discussions. The United States actively participates in the Subsidies Committee to ensure the continued effectiveness of the Subsidies Agreement. More generally, the United States relies on the provisions of the Subsidies Agreement, as well as its domestic countervailing duty (CVD) law, to deter or remedy harm caused to U.S. workers and industries from distortive subsidies.

Highlights for 2009

- *Challenging China's Export Subsidies at the WTO:* USTR and Commerce continued their strong efforts to address a wide range of trade-distorting subsidies in China in 2009, both through multilateral and bilateral actions. Most notably, in a key victory for the United States, China took steps to terminate a wide range of export subsidies following the United States' initiation of WTO dispute settlement. Specifically, China repealed or modified over 90 measures providing dozens of prohibited export subsidies that were administered by central and local government authorities. These subsidies had been supporting the export of "famous brands" of Chinese merchandise and other Chinese products

throughout the world. The termination of these subsidies will help level the playing field for American firms and workers in a wide range of manufacturing and export sectors, including textiles and apparel, metal and chemical products, medicines, agricultural and food products, light manufacturing industries, health products and household electronic appliances.

- *Addressing China's Subsidies under the U.S. Countervailing Duty Law:* As of November, 2009, Commerce had completed (*i.e.*, issued final determinations) 13 CVD investigations involving imports from China. Products under investigation include several types of steel pipe (*e.g.*, oil country tubular goods), laminated woven sacks, off-the-road tires, as well as several paper and chemical products. In 2009, Commerce initiated 10 new CVD investigations on imports from China.
- *Pushing for Increased Subsidies Disciplines in the Doha Development Round:* In the continuing WTO Doha Round negotiations, as of the end of 2009, the Rules Group had finished its first full review of the Chair's 2008 draft text, as well as the Chair's fisheries subsidies "roadmap". The Group also began the process of considering whether certain provisions in the draft Antidumping Agreement text should be "transposed" into or "harmonized" with the Subsidies Agreement.
- *Working to Increase Transparency in the WTO Subsidies Committee:* In the WTO's Subsidies Committee, the United States played an active role in the successful efforts to improve the timeliness and completeness of subsidy notifications and to enhance transparency as to a range of Members' reporting obligations, including CVD actions.
- *Defending U.S. Interests in Foreign Countervailing Duty Cases:* In 2009, USTR and Commerce defended U.S. interests in several subsidy investigations that involved exports of products from the United States. These included CVD proceedings begun in the European Union, China and Peru.

Looking Forward

Through its subsidies enforcement program, the U.S. Government is committed to identifying and challenging those unfair foreign government practices that distort international trade and thereby threaten or cause harm to American workers and companies, whether domestically or in foreign markets. Where possible, we will work to resolve these issues through advocacy, negotiation or bilateral and multilateral contacts. In those instances, however, where our interests cannot be adequately addressed through advocacy and negotiation, we will not refrain from initiating WTO dispute settlement proceedings.

In 2010, the United States will continue to vigorously enforce and defend the U.S. CVD law to protect the interests of American industries and workers unfairly harmed by subsidized imports. The United States will also continue to pursue an aggressive affirmative agenda in the Doha Round, consistent with the negotiating objective established by Congress to preserve the effectiveness of the trade remedy rules, and will press for an ambitious outcome in the fisheries subsidies negotiations. Only a dynamic and competitive global economy that remains free of the most trade-distorting types of subsidies will ensure that U.S. industries, workers and consumers enjoy the benefits that an open and competitive global economy can offer.

INTRODUCTION

The Subsidies Agreement establishes multilateral disciplines on the use of subsidies and provides mechanisms for challenging government measures that contravene these disciplines. The disciplines established by the Subsidies Agreement are subject to dispute settlement procedures, which specify 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, or the elimination of a subsidy's adverse effects. In addition, the Subsidies Agreement sets forth rules and procedures to govern the application of CVD measures by WTO Members with respect to subsidized imports.

The Subsidies Agreement nominally divides subsidy practices into 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, but are actionable (through CVD or dispute settlement action) if they are (i) "specific", *i.e.*, limited to a firm, industry or group thereof within the territory of a WTO Member and (ii) found to cause adverse trade effects, such as material injury to a domestic industry or serious prejudice to the trade interests of another WTO Member. With the expiration of the Agreement's provisions on green light subsidies, at present, the only non-actionable subsidies are those that are not specific, as defined above.¹

U.S. trade policy responses to the problems associated with foreign subsidized competition provide USTR and Commerce with both unique and complementary roles. In general, it is USTR's role to coordinate the development and implementation of overall U.S. trade policy with respect to subsidy matters; represent the United States in the WTO, including its Subsidies Committee; and chair the interagency process on matters of trade policy.

The role of Commerce, through the International Trade Administration's Import Administration (IA), is to enforce the CVD law, monitor the subsidy practices of other countries, and provide the technical expertise needed to analyze and understand the impact of foreign subsidies on U.S. commerce. In addition, USTR and IA also defend U.S. interests in CVD proceedings brought by other WTO Members against U.S. exports. IA

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 be treated as non-actionable subsidies. In addition, Article 6.1 of the Agreement provided that certain other subsidies (*e.g.*, subsidies to cover a firm's operating losses), referred to as dark amber subsidies, could be presumed to cause serious prejudice. If such subsidies were challenged on the basis of these dark amber provisions in a WTO dispute settlement proceeding, the subsidizing government would have the burden of showing that serious prejudice had *not* resulted from the subsidy. However, these provisions expired on January 1, 2000, because a consensus could not be reached among WTO Members on whether to extend them.

also works with USTR to engage foreign governments on subsidies issues when warranted. Within IA, subsidy monitoring and enforcement activities are carried out by the Subsidies Enforcement Office (SEO). (See Attachment 1). IA also provides assistance and advice to interested U.S. parties concerning the remedies available under the Subsidies Agreement and the procedures relating to these remedies and, where warranted, recommends action to USTR.

Among the joint responsibilities assigned to USTR and Commerce, as set forth in section 281(f)(4) of the Uruguay Round Agreements Act (URAA), is the submission of an annual report to the Congress describing the U.S. monitoring and enforcement activities throughout the previous year. This is the fifteenth annual report to the Congress.

MULTILATERAL INITIATIVES

A. WTO Negotiations

1. Introduction

At the Doha Ministerial Conference in 2001 – which launched the Doha Development Agenda (DDA) – Ministers agreed to negotiations aimed at clarifying and improving disciplines under the Subsidies Agreement and the WTO Agreement on Implementation of Article VI of the GATT 1994 (the Antidumping Agreement, or AD Agreement) and to address trade-distorting practices that often give rise to CVD and antidumping duty (AD) proceedings. This agreement – hereafter referred to as the Rules Mandate – also calls for clarified and improved WTO disciplines on fisheries subsidies. Under this mandate, the United States has continued to pursue an aggressive, affirmative agenda, aimed at strengthening the rules and addressing the underlying causes of unfair trade practices.

The existing WTO disciplines on subsidies prohibit only two types of subsidies: subsidies contingent upon export performance (export subsidies) and subsidies contingent upon the use of domestic over imported goods (import substitution subsidies). However, other types of permitted subsidies can significantly distort trade. The specific language of the mandate agreed to at the Doha Ministerial Conference is particularly important because it provides an avenue to address these other practices and to inform the discussions of trade remedies in a constructive manner. Moreover, it provides a basis to take up the negotiating objectives that Congress had previously laid out in the Trade Act of 2002, as well as other subsidy concerns that affect key sectors of the U.S. economy.

Another important component of the DDA is the work on disciplines specifically related to fisheries subsidies, a subject that is included as part of the Rules Mandate. The U.S. position is that the depleted state of the world's fisheries stock is a major economic and environmental concern, and that subsidies that contribute to overcapacity and overfishing, or that have other trade-distorting effects, are a significant part of the problem. The inclusion of fisheries subsidies in the Rules Mandate represents a significant

opportunity for all countries to advance simultaneously the goals of trade liberalization, environmental protection, and economic development.

2. Rules Group Background

The Negotiating Group on Rules (Rules Group) has based its work primarily on written submissions from Members, organizing its work into the following categories: (1) AD (often including issues that are relevant to CVD remedies); (2) subsidies, including fisheries subsidies; and (3) regional trade agreements. Since the Rules Group began its work in 2002, Members have submitted over 200 formal papers and over 240 elaborated informal proposals to the Group.²

At the Hong Kong Ministerial Conference in December 2005, Ministers directed the Rules Group to intensify and accelerate the negotiating process in all areas of its mandate, on the basis of detailed textual proposals. On fisheries subsidies, Ministers acknowledged broad agreement on the need for stronger rules, including a prohibition of the most harmful subsidies contributing to overcapacity and overfishing, and appropriate and effective special and differential treatment for developing country Members. Ministers also directed the Chairman of the Rules Group to prepare consolidated texts of the AD and Subsidies Agreements, taking account of progress in other areas of the negotiations.

In November 2007, the Chairman of the Rules Group, Ambassador Guillermo Valles Galmes of Uruguay, issued *Draft Consolidated Chair Texts of the AD and SCM Agreements (2007 text)*.³ The subsidies and CVD-related text was in the form of proposed revisions to the existing Subsidies Agreement, and covered a broad range of subsidy and CVD-related issues, including: subsidy calculation methodologies, dual pricing and regulated pricing practices, state-owned banking practices, export credits and rules of subsidy benefit pass-through. In the Chairman's own words, those first consolidated draft texts were intended to be "ambitious arbitrated texts, with no brackets or alternatives, addressing a wide range of critical issues, suggesting trade-offs, and proposing an overall possible solution."⁴

During the subsequent discussions of the Rules Group in 2008, however, it became clear that many Members were dissatisfied with the balance of key controversial proposals reflected in the 2007 text. At the time, the United States publicly stated that while it was very disappointed with important aspects of the 2007 text, it believed that the text provided a basis for further negotiations. Other Members expressed similar views.

² Both types of Rules papers are publicly available on the WTO website (<http://wto.org>): the formal papers may be found using the "TN/RL/W" document prefix, and the elaborated informal proposals may be found using the "TN/RL/GEN" prefix.

³ TN/RL/W/213 (November 30, 2007).

⁴ A useful summary of the DDA Rules negotiations by Chairman Valles can be found in TN/RL/W/246 (November 27, 2009).

After Ministers reached an impasse in July 2008 on how to advance the DDA in other areas, work in the Rules Group remained relatively quiet until December 18, 2008, when the Chairman issued *New Draft Consolidated Chair Texts of the AD and SCM Agreements* (2008 text).⁵ In a cover note to the 2008 text, the Chairman noted that this new document reflected a “bottom-up approach” and included new draft language on AD and subsidies/CVD issues only in those areas where some degree of convergence among the Members appeared to exist. With respect to more contentious issues for which the Chairman felt that he had no basis to propose compromise solutions or drafting language, the document simply identified those issues in brackets, along with a general summary of the range of Members’ views regarding those issues. The Chairman observed further that few, if any, of the areas in which new draft language has been proposed could be characterized as having consensus support. The Chairman has continued to make clear throughout that, whether in brackets or not, all issues remain on the table. As to the fisheries subsidies negotiations, the Chair issued a roadmap, consisting of numerous discussion questions, to further elicit Members’ views on the critical issues.

3. Major Issues and Developments in 2009

a. Subsidies/CVDs:

The Rules Group met six times throughout 2009 to discuss the Chair’s 2008 text. The Chair generally followed a “three pillars” organizational approach according to which each meeting covered a selection of: (1) bracketed proposals (*i.e.*, the most contentious), (2) un-bracketed draft textual provisions, and (3) proposals previously made by Members, but not addressed in the draft text. The key bracketed proposals discussed were: low-cost financing (*i.e.*, state-owned banking practices), export credit benchmarks, export credit successor undertakings and export competitiveness. The major un-bracketed issues covered were: dual/regulated pricing, subsidy benefit pass-through and subsidy allocation rules. “Unaddressed” issues included: withdrawal of a subsidy, appropriate interest rate benchmarks for subsidy calculations and duty drawback rules.

The Chair’s 2008 draft text makes only limited changes to the existing Subsidies Agreement, but it does include some important clarifications. For example, the 2008 text firmly establishes that the amount of a subsidy should be calculated based upon the “benefit-to-recipient” approach, an approach long advocated by the United States in all areas except for export credits (where the existing Subsidies Agreement text, in the United States’ view, explicitly establishes a cost-to-government approach). The 2009 discussions demonstrated that, in principle, these clarifications are not fundamentally controversial, although the United States and others suggested several technical refinements. The provisions in the Chair’s text on subsidy allocation methodologies – derived from a U.S. proposal – largely represent a technical advancement in the rules and were generally well-received. On the other hand, the issues of dual/regulated pricing and state-owned banking practices have been clearly much more contentious, even though the former issue was treated as a less controversial topic initially by the Chair. In the area of export credits,

⁵ TN/RL/W/236 (December 18, 2008).

many Members, including the United States, expressed serious reservations regarding the provisions in the Chair's proposed text as it would significantly change certain rules that were developed over time and that have functioned reasonably well. As a general matter, during the year, the United States continued to express concern that the 2008 text would result in insufficient strengthening of the current general subsidy disciplines, despite the Doha Rules negotiating mandate to clarify and improve the rules and address trade-distorting practices.

In September 2009, the Rules Group began the process of considering whether certain provisions in the Antidumping Agreement and the Chair's draft antidumping text should be "transposed" into or "harmonized" with the Subsidies Agreement. The initial phase of this exercise examined whether existing differences between the Antidumping and Subsidies Agreements are justified by inherent distinctions between the antidumping and CVD remedies and if not, whether the differences are appropriate topics for possible transposition/harmonization. By the end of the year, the Rules Group finished its initial review of all the differences between the two existing agreements, but though a range of views was expressed, no definitive conclusions were reached. The second phase of this exercise will begin in 2010 with the Rules Group discussing unbracketed language that currently appears in the Chair's draft antidumping text that may also be relevant to countervailing duty proceedings.

b. Fisheries Subsidies:

As part of the Doha Rules mandate, Members have committed to negotiations that "aim to clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries." The United States views the negotiations on fishery subsidies as a groundbreaking opportunity for the WTO to show that trade liberalization can benefit the environment and contribute to sustainable development as well as address traditional trade concerns. The United States has played a major role in advancing the discussion of fisheries subsidies reform in the Rules Group, working closely with a broad coalition of developed and developing countries, including Argentina, Australia, Chile, Ecuador, New Zealand and Peru (collectively known as the "Friends of Fish").

Discussions in 2009 focused on the questions contained in the Chair's "roadmap," geared off of elements of the draft text issued by the Chair in November 2007. That text sets out a broad range of prohibited subsidies that contribute to fleet overcapacity and overfishing in wild marine capture fisheries, as well as a prohibition of subsidies that affect fishing on "unequivocally overfished" stocks. The text also provides for a limited list of general exceptions available to all Members and additional exceptions for developing countries. Subsidies under both sets of exceptions would remain actionable under the existing Subsidies Agreement. In addition, the text requires Members not to cause depletion of or harm to, or create overcapacity with respect to, the fisheries resources of another Member. Finally, the text contains provisions concerning fisheries management

systems, peer review through the UN Food and Agricultural Organization (FAO), notification and surveillance of Members' fisheries subsidies, dispute settlement, and transition arrangements.

The roadmap discussions were completed at the December 2009 meeting. The discussions were generally constructive, and some progress was made on technical issues (for example, clarifying the core elements of a fisheries management system that must be in place as a condition for granting most subsidies). However, the discussions produced little movement in fundamental positions. The United States and other Friends of Fish (including Australia, Argentina, Chile, Ecuador, Mexico, New Zealand and Peru) coordinated on a joint statement supporting the high level of ambition in the Chair's text, including a broad prohibition on subsidies. Japan, Korea, Chinese Taipei and the European Union continued to object to the scope of the Chair's prohibition, particularly with respect to subsidies to cover operating costs such as fuel.

The issue of appropriate and effective treatment for developing countries was an important focus of the roadmap discussions, as well as of the negotiations overall, and continued to prove very difficult. The Chair's text provided considerable flexibility for subsistence level and small-scale developing country fishing, while limiting exceptions for developing countries to fishing activities within each country's Exclusive Economic Zone. Brazil, with support from China, Ecuador and Mexico, argued that developing country flexibilities must be extended to include fishing activities on the high seas. India pressed for greater flexibilities for its large poor population engaged in fishing. Given the prominence of developing countries in the global fishing industry, these positions among the major developing country players have the potential to create large carve outs that could undermine the objective of the negotiations to curb subsidies promoting overcapacity and overfishing.

c. Prospects for 2010

As of the end of 2009, the Rules Group had finished its first full review of the bracketed and un-bracketed horizontal subsidies issues in the 2008 draft text, as well as its discussion of the roadmap with respect to fisheries subsidies. The Chairman has signaled that, in 2010, the work program of the Rules Group will turn back to any new, additional proposals Members may want to submit. The Chairman has also made clear, however, that all issues remain on the table. It is not clear at this time when or in what form the Chairman may issue any future draft texts, although the timing of any such document will presumably be informed by progress in the DDA overall.

Throughout any future discussions, the United States will continue to pursue an aggressive affirmative agenda consistent with the negotiating objective established by Congress to preserve the effectiveness of the trade remedy rules. In the fisheries subsidies negotiations, the United States will continue to press for an ambitious outcome and work to further improve and refine many of the provisions included in the Chairman's 2007 text.

B. Steel: Multilateral Efforts to Address Market-Distorting Practices

Throughout 2009, the United States continued its multilateral efforts to address concerns related to the rapidly changing trade situation in the global steel sector, particularly through its work at the OECD and within the North American Steel Trade Committee (NASTC).

The United States is an active participant in the OECD Steel Committee (Steel Committee) and has worked closely with the Steel Committee's Secretariat, as well as the governments of other steel-producing economies, to take up policy issues affecting the global steel industry. The Steel Committee covered a broad range of issues in 2009, including government subsidies and other trade policy issues in the steel sector, raw materials policies, governmental trade-distorting practices on key steel-making inputs, and environmental issues. The lingering effects of the economic downturn on the global steel market, along with stimulus and other responses of governments to the downturn, were central to the Committee's discussions.

The NASTC continued to be a valuable forum for the governments and steel industries of North America to examine and pursue common policy approaches to promote the competitiveness of North American steel producers. The NASTC developed a North American Steel Strategy in 2006 that includes cooperation on issues of importance to steel in multilateral fora (e.g., the OECD Steel Committee and the WTO Rules Negotiations). In 2009, these cooperative efforts included coordinated interventions in the OECD Steel Committee urging governments of all steel-producing nations to refrain from the use of administrative measures to control or otherwise influence trade in steel-making raw materials. In the context of the NASTC, the governments of Canada, Mexico and the United States provided joint comments to China regarding its plans to amend its national Iron and Steel Industry Development Policy. The joint submission expressed concern regarding Chinese government policies that distort global steel and raw materials markets. The NAFTA governments called on China to eliminate subsidies to the steel industry and commit to enterprise-driven, market-based decision-making and financing for capacity expansion, and to eliminate the use of differential VAT rebates and export taxes for closely related steel products. In addition, under the NASTC, the three North American governments and steel industries have been tracking developments in certain steel-producing countries to identify, corroborate and address, as appropriate, trade-related concerns and distortions in the global steel market.

Bilaterally, at the OECD and in the WTO, the United States continued to raise specific concerns with other countries about steel policies that contribute to excess capacity and production, including subsidies, border measures on steel and steelmaking raw materials, and other trade-distorting practices. The United States also continued to oppose support by national and multilateral financial institutions for projects that increase raw or finished steel capacity.

MONITORING AND ENFORCEMENT

A. Advocacy Efforts and Monitoring Subsidy Practices Worldwide

Identifying, researching and evaluating potential foreign government subsidy practices is a core function of the subsidies enforcement program. Experienced analysts in IA, with various foreign language skills, primarily conduct this work, which involves daily searches of worldwide business journals, periodicals, various online resources, utilization of numerous legal databases and ongoing relationships with U.S. industry contacts. IA officers stationed overseas (for example, in China) enhance these efforts by helping to gather, clarify, and check the accuracy of information concerning foreign subsidy practices.

USTR and IA staff continued their activities to monitor market- and trade-distorting practices by governments worldwide in 2009. A key example, which is described in more detail below, is the extensive year-long research that led to the discovery of the wide-spread use of prohibited export subsidies by Chinese governments at the national and sub-national levels.

1. Counseling U.S. Industry

USTR and IA regularly work with U.S. companies concerned about the subsidization of foreign competitors. The goal is to resolve problems through a combination of informal and formal contacts. The United States will also advise U.S. companies of other options, such as a CVD investigation or WTO dispute settlement.

USTR and IA work closely with affected companies to collect information concerning potential subsidies and to determine how their commercial interests may have been harmed. While companies facing subsidized competition can usually provide good information as to the financial health of their industry, assistance is often needed to obtain additional information regarding the alleged subsidy practices in question. In these instances, USTR and IA conduct additional research to determine the legal framework under which a foreign government may be offering potential subsidies and whether other U.S. firms or industries have been facing similar problems.

Working with an interagency team, USTR and IA analyze the information and determine the most effective way to proceed. It is often advantageous to pursue resolution of these problems by raising the matter with the foreign government authorities through informal contacts, formal bilateral meetings or through discussions in the WTO Subsidies Committee. This process may produce more expeditious and practical solutions to the problem than would immediate recourse to WTO dispute settlement or the filing of a CVD petition. If these informal efforts fail to resolve adequately the issue, the U.S. government may consider initiating WTO dispute settlement proceedings or may advise an affected firm about procedures for filing a CVD petition.

During 2009, USTR and Commerce worked with a broad array of U.S. industries and companies that had significant concerns about unfair foreign government subsidy

practices in a wide range of countries. These activities included new and ongoing work on behalf of the U.S. aerospace, aluminum, chemical, paper, steel and textile industries among others. The subsidy practices examined included those maintained by the central and local governments of Brazil, Canada, China, the European Union, India, Indonesia, Japan, Mexico, Pakistan, South Africa, South Korea, Turkey and Vietnam.

2. Outreach Efforts

USTR and IA coordinate with other U.S. government personnel who have direct contact with the U.S. exporting community, both in the United States and abroad, to make them aware of the resources and services available regarding subsidy enforcement efforts. For example, USTR and IA personnel train Department of State and Department of Agriculture officers on how to identify and evaluate foreign subsidy practices. This collaboration among U.S. government agencies, each with its own on-the-ground knowledge and expertise, is important to help effectively exercise U.S. rights under the Subsidies Agreement. Also, as noted, USTR and IA maintain staff in some overseas posts (*i.e.*, in Beijing and Geneva). Working closely with their colleagues in U.S. embassies and IA personnel in Washington, the IA officers stationed in Beijing undertake primary source research of potential unfair trade problems in China and in other countries in the region. Furthermore, a senior IA officer stationed in Geneva, Switzerland, has been an active participant in the ongoing WTO Rules negotiations and in the WTO Antidumping, Safeguard and Subsidies Committees and also monitors dispute settlement activities.

Technical exchanges on trade remedy issues continued to be an important aspect of U.S. outreach activities with foreign government officials in 2009. During the past year, IA organized and participated in many of these exchanges, including with officials from Brazil, the European Union, Indonesia, Laos, Thailand and Ukraine. These technical exchanges promote a better understanding of other countries' trade remedy practices and allow a more fulsome evaluation of how other countries are complying with their WTO obligations. Technical exchanges have also provided the opportunity to encourage "best practices", strengthen ties with other trade remedy administrators, and foster increased transparency.

3. Electronic Subsidies Enforcement Library

The "Electronic Subsidies Enforcement Library" (ESEL) website is a key tool used by IA to organize subsidy-related material and convey it to the public. The website -- available at <http://esel.trade.gov> -- includes foreign governments' subsidies notifications made to the WTO, an overview of the SEO, information on U.S. AD/CVD proceedings as well as AD/CVD actions with respect to U.S. exports, helpful links, and an easily navigable tool that provides information about each subsidy program investigated by Commerce in CVD cases since 1980. (See Attachment 2). The website is updated to provide the most recently available information to the public in a timely manner. During 2009, IA invested in new software for the ESEL, significantly improving the user interface and search functions.

B. CHINA

1. WTO Transitional Review Mechanism (TRM)

In October 2009, the United States took part in the eighth annual transitional review with respect to China's implementation of its WTO obligations, which is a review mandated by paragraph 18 of Part I of China's Protocol of Accession to the WTO. Paragraph 18 provides that all subsidiary bodies, including the Subsidies Committee, "which have a mandate covering China's commitments under the WTO Agreement or [the] Protocol shall, within one year after accession . . . review, as appropriate to their mandate, the implementation by China of the WTO Agreement and of the related provisions of [the] Protocol." Paragraph 18 further states that such reviews shall be conducted on an annual basis for eight years, with a final review occurring by the tenth year after accession.

Upon its accession to the WTO, China agreed to assume the obligations of the WTO Subsidies Agreement. As part of its accession agreement, China committed that it would eliminate, by the time of its accession, all subsidies prohibited under Article 3 of the Subsidies Agreement, *i.e.*, export subsidies and import substitution subsidies. The Subsidies Agreement also requires that China, like all other WTO Members, notify all of its subsidies that are specific, whether maintained by the national or sub-national governments.

China also agreed to various special rules that apply when other WTO Members seek to enforce the disciplines of the Subsidies Agreement against Chinese subsidies (either through domestic CVD proceedings or in WTO enforcement proceedings). These rules permit WTO Members, in certain circumstances, to identify and measure Chinese subsidies using alternative methods in order to account for the special characteristics of China's economy. For example, special rules govern the actionability of subsidies provided to state-owned enterprises (SOEs).

As a result of pressure from the United States and other WTO Members, China submitted its first subsidies notification to the WTO's Subsidies Committee in April 2006. Although the notification covered over 70 subsidy programs, it omitted numerous programs and failed to include any subsidies provided by provincial and local government authorities. During the transitional review before the Subsidies Committee in October 2009, the United States reiterated its concerns as to the lack of provincial and local programs in China's subsidy notification and raised several other issues, including export-contingent subsidies, industrial subsidy policy administration, government assistance in the textile and civil aerospace sectors, price controls on fuels, and land administration.

The United States has devoted significant time and resources to researching, monitoring and analyzing China's subsidy practices, which has helped to identify the very significant omissions in China's subsidy notification and lay the groundwork for the further pursuit of issues in the context of the Subsidies Committee's work and WTO dispute settlement (see, for example, the *Dispute Settlement* section below). During the transitional review, China stated it is in the final stages of its internal review with respect to

its next subsidy notification. Unfortunately, however, China also stated that this next notification will not include information on provincial and local programs. In light of the importance of this information, the United States will have to consider alternative approaches to address this outstanding issue.

In 2010, the United States will continue to focus on China's subsidy programs, particularly those programs not notified and those programs administered at the provincial and local levels that may raise questions of consistency with the Subsidies Agreement. Assuming China submits a new subsidy notification, the United States will closely scrutinize it and may bring to the notice of the Committee unreported subsidies, particularly subsidies at the provincial or local level.

2. Dispute Settlement-Grants, Loans and Other Incentives

As discussed above, on December 19, 2008, the United States and Mexico requested consultations with China regarding government support tied to China's industrial policy to promote the sale of Chinese brand name (e.g., "famous export brand") and other products abroad. Guatemala joined the dispute on January 19, 2009.

The consultation requests addressed central government initiatives promoting famous Chinese brands of merchandise and dozens of sub-central government measures implementing these initiatives. For example, at the central government level, China established the "Famous Export Brand" initiative, the "China World Top Brand" initiative, and the "China Name Brand Products" initiative. These measures set out criteria for an enterprise to receive a designation by the Ministry of Commerce (MOFCOM) as a "Famous Export Brand" or a designation by the Administration of Quality Supervision, Inspection and Quarantine (AQSIQ) as a "China World Top Brand" or "China Name Brand Product." Enterprises with these designations were entitled to various government preferences, including, it appeared, financial support tied to exports.

The consultation request also addressed several independent sub-central government subsidy programs that appeared to benefit Chinese exports regardless of whether they were famous brands. Certain of the measures were targeted at a more defined set of export sectors (or to a single sector), including the high-technology, electromechanical, textiles, and agricultural sectors.

All of the challenged initiatives appeared to qualify as export subsidies, because they were granted on the condition that the recipients meet certain export performance criteria. As previously explained, export subsidies are generally prohibited under the Subsidies Agreement.

China's lone subsidies notification to the WTO, submitted in April 2006, did not identify any of the measures at issue in this case and, as noted above, did not provide any information about subsidy programs maintained by sub-central levels of government. As a result, the famous export brand and other product subsidies at issue in this case had to be uncovered through significant investigatory work by the U.S. Government, working with

U.S. industry. The United States ultimately identified more than 90 separate official measures, issued and applied by various levels of government in China, providing what appeared to be WTO-inconsistent financial support.

Following consultations in Geneva in February 2009, the United States, Guatemala, and Mexico worked intensively and cooperatively with China to reach a solution to the dispute without resort to panel proceedings at the WTO. By November 2009, the parties were able to finalize an agreement in which China confirmed that it had taken steps over the preceding months to eliminate the measures of concern or to modify them to remove any provisions related to export-contingent brand designations and financial benefits.

The termination of the subsidies represents a key victory for the United States because it will level the playing field for American workers and businesses in a wide range of manufacturing and export sectors, including textiles and apparel, metal and chemical products, light manufacturing industries, agricultural and food products, medicines, health products and household electronic appliances.

3. Application of Countervailing Duty Law to China

In 2007, based on a CVD petition filed by the U.S. coated free sheet paper industry, the Commerce Department changed its longstanding policy of not applying U.S. CVD law to China. Commerce changed its policy and began applying the CVD law to China after finding that reforms to China's economy in recent years had removed the obstacles to applying the CVD law that were present in the "Soviet-era economies" at issue when the Commerce Department first declined to apply the CVD law to NMEs in the 1980s.

Since then, several other U.S. industries concerned about subsidized Chinese imports have filed CVD petitions, and the Department initiated 10 new investigations in 2009. Through January 2010, the Commerce Department reached final affirmative CVD determinations concerning imports from China of laminated woven sacks, circular and rectangular pipe, off-the-road tires, thermal paper, sodium nitrate, pressure pipe, line pipe, citric acid, lawn groomers, kitchen racks and oil country tubular goods. Ongoing CVD investigations of Chinese exports of wire decking, steel grating, phosphate salts, seamless pipe, pre-stressed concrete steel wire strand, carbon bricks, coated paper and drill pipe are scheduled to be completed in 2010. The alleged subsidies being investigated include preferential government policy loans, income tax and VAT exemptions and reductions, the provision of goods and services such as land, electricity and steel on non-commercial terms, and a variety of provincial and local government subsidies.

4. JCCT - Structural Issues Working Group (SIWG) and the Trade Remedies Working Group (TRWG)

Established in 1983, the U.S.-China Joint Commission on Commerce and Trade (JCCT) is a government-to-government consultative mechanism that provides a forum to resolve trade concerns and promote bilateral commercial opportunities. In 2009, the JCCT was chaired by Secretary Locke and Ambassador Kirk on the U.S. side and by Vice

Premier Wang Qishan on the Chinese side. Several other senior-level representatives participated on both sides.

From a U.S. trade policy standpoint, it is important to engage China regarding existing structural and operational issues regarding China's economy, particularly those that give rise to trade friction, and to encourage China's ongoing economic reform efforts. At the same time, China's status as an NME under U.S. antidumping law is of substantial concern and importance to the Chinese government. In order to better understand China's reforms to date and various structural and operational aspects of China's economy, as well as to discuss issues that relate to China's desire for market economy status under the U.S. antidumping law, China and the United States agreed during the April 2004 JCCT meetings to the establishment of a new working group, the SIWG, to be jointly chaired by Commerce's Assistant Secretary for Import Administration and the Assistant U.S. Trade Representative for China Affairs on the U.S. side and the Director General of MOFCOM's Bureau of Fair Trade on the Chinese side.

The SIWG provides a forum for the U.S. and Chinese governments to explore and discuss China's economy and its ongoing economic reform program, raise concerns about market- and trade-distorting practices (including subsidy practices) that might otherwise lead to bilateral trade frictions, and consider the Chinese government's concerns about China's NME status under U.S. antidumping law.⁶ The working group has met a number of times since its launch in July 2004, with both sides including in their delegations experts from a variety of agencies responsible for the broad range of structural/institutional issues and economic reforms/policies under discussion.

The United States and China also agreed to convene a second working group, the TRWG, in conjunction with the SIWG meetings, to serve as a forum for both sides to raise issues of concern with regard to the other's trade remedy practices and proceedings.

At the inaugural meeting of the U.S.-China Strategic Economic Dialogue (SED) in December 2006, both China and the United States agreed to invigorate discussion under the JCCT of structural issues/market economy status, with the SIWG providing the vehicle for doing so. Similar commitments were made in subsequent SED meetings, as well as during the inaugural meeting of the SED's successor, the Strategic and Economic Dialogue (S&ED), in July 2009. The latest SIWG meeting on January 21, 2010, reflected these same commitments, with an interagency delegation from China working with the United States to examine key aspects of China's reforms of property law and land use rights, as well as certain resource allocation policies, such as China's use of highly variable value-added tax rebate rates for exports.

⁶ The SIWG is not a forum for resolving or deciding this issue, but it provides a constructive setting for the mutual exchange of views and relevant information. Under U.S. law, any review of China's NME status must take place in a formal proceeding before Commerce, open to all interested parties.

C. Subsidy Programs Related to Members' Stimulus Packages

The size and scope of the economic crisis that began in late 2008 prompted numerous developed and developing countries to institute significant economic stimulus and financial sector rescue packages. Without questioning the necessity of the many support measures that have prevailed over the past year, the sheer magnitude of the government interventions poses concerns about the potential impact such support could have on international trade. The overall size of the fiscal stimulus packages in OECD countries has been estimated at 3.5 percent of collective GDP, while many emerging economies also have sizable financial stimulus packages, most notably China, Brazil and Russia. China's stimulus package is reported to be the largest in relative terms, amounting to approximately 13 percent of GDP (fiscal and financial stimulus combined).

Any thorough review and analysis of these massive economic stimulus packages can be challenging. Although temporary stimulus measures may be necessary to address the current economic crisis, governments should ensure that such measures do not violate Members' international commitments. As such, effective monitoring and evaluation of these measures is important, especially in the case of those measures that do not appear to be consistent with WTO rules governing the use of subsidies. In that regard, concerns arise in particular with respect to these support measures that are targeted at specific industrial sectors, such as textiles and steel, and that are explicitly prohibited by WTO rules, i.e., those that are contingent upon exports or that favor domestic over imported goods. During the past year, the WTO Director General and WTO Secretariat issued reports to WTO Members on trade and trade-related policy developments occurring in the context of the latest financial and economic crisis.⁷ The U.S. Government will continue to monitor WTO Members' activities in this area to ensure that they adhere to their WTO commitments when implementing policies to address economic and financial instability.

D. WTO Dispute Settlement

1. European Union Support for Airbus

For many years, the United States has had serious concerns about the continued EU subsidization of Airbus, a company with more than a 50 percent share of the world market for large civil aircraft (LCA). The subsidies for LCA have taken many forms, including "launch aid," which Airbus uses to launch new models of aircraft; grants for Airbus infrastructure; forgiveness of debt; and subsidies to underwrite Airbus' research and development costs.

U.S. concerns about Airbus subsidies intensified in 2004, when it became apparent that Airbus intended to launch a new aircraft, the A350, with yet another round of EU launch aid. On October 6, 2004, following unsuccessful, U.S.-initiated efforts to negotiate a new U.S.-EU agreement that would preclude new subsidies, the United States filed a WTO

⁷ See WTO documents, WT/TPR/OV/W/1 of April 2009, WT/TPR/OV/W/2/ of July 2009 and WT/TPR/OV/12 of November 2009.

consultation request with respect to subsidies that Airbus has received for LCA. Concurrent with the U.S. WTO consultation request, the United States also exercised its right to terminate the 1992 U.S.-EU bilateral LCA agreement.

The WTO consultations failed to resolve the U.S. concerns, and a renewed effort to negotiate a solution ended without success in April 2005. Therefore, on May 31, 2005, the United States filed a WTO panel request. The WTO Dispute Settlement Body (DSB) established a panel on July 20, 2005, and panel proceedings are currently ongoing. (Separately, and as discussed below, on October 6, 2004, the EU filed a WTO consultations request with respect to alleged U.S. federal, state and local government subsidies to Boeing. The EU's complaint is pending before a different WTO panel.) The parties have filed several written submissions, and the panel heard arguments by the parties at meetings in March and July 2007. The final panel report is expected in 2010.

2. United States Support for Large Civil Aircraft

On October 6, 2004, the EU requested consultations with respect to "prohibited and actionable subsidies provided to U.S. producers of large civil aircraft." The EU alleged that such subsidies violate several provisions of the Subsidies Agreement, as well as Article III:4 of the GATT 1994. Consultations were held on November 5, 2004. On May 31, 2005, the EU requested the establishment of a panel to consider its claims. The EU filed a second request for consultations regarding large civil aircraft subsidies on June 27, 2005. This request covered many of the measures covered in the initial consultations, as well as many additional measures that were not covered.

The EU requested establishment of a panel with regard to its second panel request on January 20, 2006. The DSB established a panel on February 17, 2006. The parties have filed several written submissions, and the panel heard arguments by the parties at meetings in September 2007 and January 2008. The panel subsequently issued two sets of written questions to the parties.

3. United States – Subsidies on Upland Cotton

On September 8, 2004, the panel in *United States—Subsidies on Upland Cotton* circulated its final report. The panel, *inter alia*, made the following findings: (1) certain export credit guarantees (under the GSM 102, GSM 103, and SCGP programs) were prohibited export subsidies; (2) some payments under U.S. domestic support programs (marketing loan, counter-cyclical, market loss assistance, and Step 2 payments) were found to cause significant suppression of cotton prices in the world market causing serious prejudice to Brazil's interests; and (3) Step 2 payments to exporters of cotton were prohibited export subsidies and Step 2 payments to domestic users were prohibited import substitution subsidies because they were contingent upon the purchase of U.S. cotton.

The United States and Brazil appealed several of the panel's findings. The Appellate Body circulated its report on March 3, 2005, upholding the panel's findings appealed by the United States. The Appellate Body also rejected or declined to make

findings on most of Brazil's arguments. On March 21, 2005, the DSB adopted the panel and Appellate Body reports and, on April 20, 2005, the United States advised the DSB that it intended to bring its measures into compliance.

On June 30, 2005, the United States announced that it would cease to issue export credit guarantees under the GSM 103 program. It also announced a new fee structure for the GSM 102 program designed to make the program more "risk-based," consistent with the original panel's findings. The United States ceased to issue guarantees under the SCGP as of October 1, 2005.

On February 1, 2006, Congress enacted legislation that repealed the Step 2 program, with an effective date of August 1, 2006.

On July 5, 2005, Brazil requested authorization to impose countermeasures in the amount of \$3 billion in connection with the "prohibited subsidy" findings. On July 14, 2005, the United States objected to the request, thereby referring the matter to arbitration. On August 17, 2005, the United States and Brazil agreed to suspend the arbitration. On October 6, 2005, Brazil made a separate request for authorization to impose countermeasures in the amount of \$1 billion per year in connection with the "serious prejudice" findings. The United States objected to Brazil's request on October 17, 2005, thereby also referring that matter to arbitration. Thereafter, on November 21, 2005, the United States and Brazil jointly requested suspension of this second arbitration.

On September 28, 2006, the WTO DSB established an Article 21.5 (compliance) panel, at Brazil's request, to review U.S. compliance with the rulings in the dispute. Brazil argued that the United States remained out of compliance with both the prohibited subsidy findings and the actionable subsidy findings. The panel circulated its final report on December 18, 2007. The panel found, *inter alia*, that: (1) export credit guarantees issued under the GSM 102 program with respect to unscheduled and certain scheduled (rice, pig and poultry meat) commodities constituted prohibited export subsidies; and (2) U.S. marketing loan and counter-cyclical payments for upland cotton were continuing to cause serious prejudice to Brazil by significantly suppressing world upland cotton prices. The panel rejected Brazil's claim that payments under the marketing loan and counter-cyclical payment programs were responsible for an increase in U.S. market share in marketing year 2005 and thereby caused serious prejudice to Brazil's interests. The panel also agreed that the United States was not required to have refused to perform on export credit guarantees that were issued prior to the deadline for the implementation of the DSB's recommendations and rulings as to such guarantees (July 1, 2005) and that were still outstanding as of that date.

The United States appealed the compliance panel's adverse findings on February 12, 2008. Brazil filed its notice of other appeal on February 25, 2008. The Appellate Body issued its report on June 2, 2008, in which it:

- upheld the compliance panel's finding that U.S. marketing loan and counter-cyclical payments cause significant price suppression in the market for upland cotton, thereby constituting present serious prejudice to Brazil;
- agreed with the United States that the compliance panel erred in dismissing U.S. Government budgetary data showing that U.S. export credit guarantee programs operate at a profit, but nonetheless upheld the compliance panel's ultimate finding that GSM 102 export credit guarantees with respect to unscheduled products and certain scheduled products (rice, pig meat, poultry meat) were prohibited export subsidies; and
- upheld the compliance panel's finding that Brazil's claims as to marketing loan and counter-cyclical payments made after September 21, 2005, and Brazil's claims as to GSM 102 guarantees for exports of pig meat and poultry meat, were within the scope of the compliance proceeding.

The DSB adopted the Appellate Body report, and the panel report, as modified by the Appellate Body report, on June 20, 2008. Brazil requested resumption of both arbitration proceedings on August 25, 2008. The meetings with the Arbitrators took place on March 2-4, 2009.

The Arbitrators issued their awards on August 31, 2009. They issued one award concerning U.S. subsidies found to cause serious prejudice to Brazil's interests (marketing loan and countercyclical payments for cotton), and another award concerning U.S. subsidies found to be prohibited export subsidies (export credit guarantees under the GSM 102 program for a range of agricultural products plus the repealed "Step 2" program for cotton).

The Arbitrators found that Brazil may impose countermeasures against U.S. trade:

- (1) for marketing loan and countercyclical payments for cotton, in an annual fixed amount of \$147.3 million, and
- (2) for export credit guarantees under the GSM 102 program, in an annual amount that may change each year based on a formula.

The Arbitrators rejected Brazil's request for countermeasures for the Step 2 program.

The Arbitrators also found that, in the event that the total level of countermeasures that Brazil would be entitled to in a given year should increase to a level that would exceed a threshold based on a subset of Brazil's consumer goods imports from the United States, then Brazil would also be entitled to suspend certain obligations under the TRIPS Agreement and/or the GATS with respect to any amount of permissible countermeasures applied in excess of that figure.

On September 25, 2009, Brazil requested data from the United States for 2008 and 2009 to calculate countermeasures according to the formula in the Arbitrator's award. On November 19, the United States provided Brazil the data requested for 2008 and stated that it would provide 2009 data when they are complete.

On November 19, 2009, the DSB granted Brazil authorization to suspend the application to the United States of concessions or other obligations consistent with the Arbitrator's awards.

4. United States Domestic Support for Agriculture

On January 8, 2007, Canada requested WTO dispute settlement consultations with the United States, alleging that: (1) support to U.S. corn producers has caused and threatens to cause serious prejudice to the interests of Canada, specifically through price suppression and depression in the Canadian corn market; (2) U.S. export credit guarantee programs for corn and all unscheduled commodities constitute prohibited export subsidies; and (3) U.S. government support for all agricultural products resulted in a breach of the U.S. scheduled cap on its Aggregate Measurement of Support (AMS) under the Agreement on Agriculture. On July 11, 2007, Brazil submitted a request for consultations that made claims similar to the second and third allegations made by Canada.

On November 8, 2007, both Canada and Brazil requested the establishment of a panel, limited to the claims that total U.S. support for agriculture breached the U.S. AMS limit in each of 1999, 2000, 2001, 2002, 2004, and 2005, contrary to the Agreement on Agriculture. More than 100 programs were identified in each panel request as allegedly providing support during the relevant years. The panel requests did not include claims under the Subsidies Agreement that had been part of the consultations request (*i.e.*, a claim of serious prejudice with respect to corn and a prohibited subsidy claim with respect to export credit guarantee programs). On December 17, 2007, the DSB established a single panel to consider both disputes. However, the panel has not yet been composed.

5. United States – Application of CVDs to China

A WTO dispute settlement panel is reviewing the compatibility with the WTO agreements of four pairs of Commerce AD and CVD determinations.⁸ China is challenging how Commerce determined the amount of countervailable subsidies in these CVD investigations, including the identification and calculation of subsidies such as policy lending and the provision of goods (including land use rights and electricity) for less than adequate remuneration. China is also raising certain procedural challenges to the determinations. In addition, China is arguing that the application of a countervailing duty in addition to an anti-dumping duty calculated pursuant to Commerce's nonmarket economy

⁸ The WTO proceeding is *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, WT/DS379. The Commerce AD and CVD determinations apply to exports from China of *Circular Welded Pipe, Off-Road Tires, Laminated Woven Sacks, and Light-Walled Rectangular Pipe*.

methodology results in a “double remedy” for domestic subsidies in China. The panel held hearings during 2009 and a confidential interim report is expected to be issued to the parties in the first half of 2010. A number of related issues are being litigated under U.S. law in the U.S. Court of International Trade.⁹

6. Canada – U.S. Softwood Lumber Agreement

The 2006 Softwood Lumber Agreement between the Government of the United States of America and the Government of Canada (SLA) was signed on September 12, 2006, and entered into force on October 12, 2006. Pursuant to a settlement of litigation, Commerce revoked the antidumping and countervailing duty orders on imports of softwood lumber from Canada. (The settlement ended a large portion of the litigation over trade in softwood lumber). Upon revocation of the orders, U.S. Customs and Border Protection ceased collecting cash deposits and returned previously collected deposits with interest to the importers of record.

The SLA provides for unrestricted trade in softwood lumber in favorable market conditions. However, when the lumber market is soft, Canada must impose export measures. Canadian exporting provinces can choose either to collect an export charge that ranges from 5 percent to 15 percent as prices fall or to collect lower export charges and limit export volumes. The SLA also includes provisions to address potential Canadian import surges, provide for effective dispute settlement, and monitor administration of the SLA through the establishment of a Softwood Lumber Committee. In addition, the SLA prohibits “circumvention” of the SLA by restricting Canada from taking any action having the effect of reducing or offsetting the export measures. The SLA specifically provides that, with certain enumerated exceptions, grants or benefits provided by a Party, including any public authority of a Party, to producers or exporters of Canadian softwood lumber products shall be deemed to reduce or offset the export measures.

On March 30, 2007, the United States requested formal consultations with Canada to resolve concerns regarding several Canadian federal and provincial programs, as well as Canada’s interpretation of provisions of the SLA that adjust softwood lumber export levels, including the level triggering the SLA’s surge mechanism. After formal consultations failed to resolve these concerns, on August 8, 2007, the United States requested international arbitration under the terms of the SLA before the London Court of International Arbitration (LCIA) to compel compliance with Canada’s obligations relating to export volume caps and proper application of the import surge mechanism. On March 3, 2008, the arbitration tribunal considering the matter determined that Canada violated its SLA obligations by failing to properly adjust quota levels during the first half of 2007. After further briefing, on February 26, 2009, the tribunal ruled that Canada had 30 days in which to either cure its breach of its SLA obligations, or impose compensatory adjustments specifically articulated by the tribunal. The tribunal stated that the compensatory adjustments were to be Canada’s application of an additional 10 percent ad valorem export charge on softwood lumber exports from its eastern provinces (Ontario, Quebec, Manitoba

⁹ The CIT litigation is *GPX v. United States*, CIT No. 08-00285.

and Saskatchewan) until it had collected U.S. \$54.8 million. In the event that it failed to comply, the SLA authorized the United States to impose customs duties in an equal amount.

On March 25, 2009, Canada stated that it did not intend to apply the export charge. Two days later, Canada offered a payment of US \$36.66 million to the U.S. Government. The United States rejected Canada's offer. On April 2, 2009, Canada requested that the arbitration tribunal be re-constituted to determine whether Canada had cured its breach of the SLA. On April 10, 2009, USTR published a notice in the Federal Register imposing a 10 percent *ad valorem* duty on imports of softwood lumber from Canada's eastern provinces, effective April 15, 2009. On June 11, 2009, the tribunal conducted a hearing to consider Canada's arguments that its payment offer cured its breach of the SLA. The tribunal issued a decision on September 30, 2009, in which it found that Canada's payment offer did not cure its breach of the SLA. CBP continues to collect import duties. Canada has indicated that it desires to implement the tribunal's ruling and transfer responsibilities from the United States to Canada for collecting the remainder of the \$54.8 million. The United States has posed a number of questions to Canada concerning the details of such a transfer, including the authority of the Government of Canada to collect the additional export charge. The United States is considering Canada's responses to its questions and continues to work with Canada on bringing this matter to resolution.

On January 18, 2008, the United States requested a second arbitration before the LCIA to address U.S. allegations that Ontario and Quebec had implemented a total of six programs that benefited the lumber industry in violation of the anti-circumvention provisions of the SLA. Following the submission of written briefs, an LCIA tribunal conducted a hearing in Ottawa, from July 17 through 21, 2009, to consider the issues of liability and remedy. After the hearing, Canada and the United States filed post-hearing briefs, as requested by the tribunal. On January 21, 2010, the tribunal requested additional submissions from the parties' economic experts on the benefits provided by certain programs and the reduction or offset of the export measures caused by such benefits. The tribunal asked the experts to file a joint report, if possible, or separate reports by March 18, 2010, and the parties may file written comments on the report(s) by April 15, 2010. Another hearing on remedy may be held following the written submissions, and we expect a decision from the tribunal in mid-2010.

On June 18, 2008, Congress enacted the Softwood Lumber Act of 2008. Among other things, the Act requires Commerce, every 180 days, to provide the "appropriate congressional committees a report on any subsidies on softwood lumber . . . provided by countries of export." As of December 31, 2009, Commerce had submitted three reports to the Senate Finance and House Ways and Means Committees, and placed copies of each report on the agency's website.

E. Countervailing Duty Investigations on Exports from the United States

In 2009, USTR and Commerce worked diligently to defend U.S. commercial interests in several subsidy investigations that involved exports of products from the United States. These included CVD proceedings conducted in the European Union, China and Peru.

1. European Union

In 2008, the European Commission initiated two countervailing duty investigations on imports of products from the United States. The first investigation was initiated on June 13, 2008, and involved biodiesel exports from the United States. Several alleged state and federal government programs were included in the investigation. USTR and Commerce worked closely with the states, other federal government agencies and U.S. industry to respond to Commission questionnaires and participate in the verification of the questionnaire responses. Despite the efforts on the part of USTR and Commerce, in July 2009, the Council of the European Union adopted definitive countervailing duties on imports of biodiesel from the United States. The countervailing duty rates ranged from EUR 211 to EUR 237 per ton.

On July 23, 2008, the European Commission initiated a countervailing duty investigation of sodium metal from the United States. The alleged subsidy related to the pricing of hydroelectric power generated at Niagara Falls and supplied by the New York Power Authority (NYPA) to the sole U.S. producer of sodium metal. USTR and Commerce worked closely with NYPA, New York state officials, and U.S. industry to respond to Commission questionnaires and participate in the verification of questionnaire responses. The petition was eventually withdrawn by MSSA SAS, the sole France-based EC producer of sodium metal, after a settlement was reached with the U.S. producer of sodium metal. As a result, the Commission terminated the investigation in June 2009.

2. China

In June 2009, acting on a petition from Chinese steel producers, MOFCOM initiated China's first CVD investigation. The petition alleged that U.S. federal and state governments have provided subsidies to U.S. producers of grain-oriented electrical steel (GOES). Since then, MOFCOM has initiated two additional CVD investigations involving imports of chicken parts and automobiles from the United States. The preliminary determination in the GOES investigation was issued in December 2009. MOFCOM found several of the alleged programs to be countervailable, including the Buy America Act and three state programs. The rates applied were between 11.7 and 12 percent. The final determination is expected in May 2010. The preliminary determinations in the chicken parts investigation and the automobiles investigation are expected to be released in the first half of 2010.

Through these investigations, it has become evident that China needs to improve the transparency and procedural fairness of its CVD proceedings. These investigations

raise a number of questions regarding the actions of MOFCOM and consistency with WTO rules. These include issues such as whether there was sufficient evidence to initiate these investigations, whether sufficient time for responses was provided, whether conclusions drawn were supported by evidence, and whether the use of facts available was warranted.¹⁰

The United States has raised its concerns bilaterally with MOFCOM as well as at the WTO in regular meetings before the Subsidies and Antidumping Committees. The United States has also fully cooperated in MOFCOM's ongoing CVD investigations in order to safeguard the interests of U.S. industry and to ensure that China fully complies with the Subsidies Agreement rules.

3. Peru

On August 26, 2009, the Government of Peru initiated an anti-subsidy investigation on exports of biodiesel from the United States. The petition alleged two federal tax programs that currently are the subject of the investigation. USTR and Commerce worked closely with other federal government agencies to respond to Peru's initial questionnaire. On December 17, 2009, the Government of Peru issued a resolution to impose provisional countervailing duties in the amount of \$178 per ton on imports of U.S. biodiesel. The final determination in this case is expected to be issued no later than May 2010.

F. WTO Subsidies Committee

The Committee on Subsidies and Countervailing Measures (Subsidies Committee) held two formal meetings in 2009, in May and October, and held informal meetings in March, July and October. The Subsidies Committee continued its regular work of reviewing Members' notifications of their subsidy programs to the Subsidies Committee, as well as the consistency of Members' domestic laws, regulations, and actions with the Subsidies Agreement's requirements. Importantly, the Subsidies Committee adopted modifications to its reporting formats in order to improve the timeliness and completeness of notifications. As discussed above, during the October meeting, the Subsidies Committee held its eighth review of China's implementation of the Subsidies Agreement, pursuant to the Transitional Review Mechanism provided by China's protocol of WTO accession. Other items addressed in the course of the year included: examination and approval of specific export subsidy program extension requests for certain small economy developing country Members; election of Mr. Gerard Depayre (France) to the five-member Permanent Group of Experts; and updating the eligibility threshold for developing countries to provide export subsidies under Annex VII(b) of the Subsidies Agreement. Further information on these various activities is provided below.

¹⁰ Under certain circumstances, if a party refuses to provide necessary information, an investigating authority may use the facts otherwise available in reaching the applicable determination.

1. Subsidy Notifications by Other WTO Members

Subsidy notification and surveillance is one means by which the Subsidies Committee and its Members seek to ensure adherence to the disciplines of the Subsidies Agreement. In keeping with the objectives and directives expressed in the Uruguay Round Agreements Acts, WTO subsidy notifications also play an important role in the U.S. monitoring and enforcement activities under the Subsidies Agreement.

Under Article 25.2 of the Subsidies Agreement, Members are required to report certain information on all measures, practices and activities that, as set forth in Articles 1 and 2 of the Agreement, meet the definition of a subsidy and are specific within the territory of a Member. In 2009, four 2009 and eleven 2007 subsidy notifications¹¹ were reviewed. Unfortunately, numerous Members have never made a subsidy notification to the WTO, although many are lesser developed countries.¹²

2. Review of CVD Legislation, Regulations and Measures

Throughout 2009, WTO Members continued to submit notifications of new or amended CVD legislation and regulations, as well as CVD investigations initiated and decisions taken. These notifications were reviewed and discussed by the Committee at both of its regular meetings. In reviewing notified CVD legislation and regulations, the Committee procedures provide for the exchange in advance of written questions and answers in order to clarify the operation of the notified laws and regulations and their relationship to the obligations of the Agreement. The United States continued to play an important role in the Committee's examination of the operation of other Members' CVD laws and their consistency with the obligations of the Agreement.

To date, 90 Members¹³ of the WTO have notified that they have CVD legislation in place, and 36 Members have notified that they have no CVD legislation in place. Among the notifications of CVD laws and regulations reviewed in 2009 were those of Argentina, Brazil, Ukraine, and the United States.

As for CVD measures, nine WTO Members notified CVD actions taken during the latter half of 2008, and eleven Members notified actions taken in the first half of 2009. The

¹¹ During the 2009 Spring and Fall Subsidies Committee Meeting, the Committee discussed the 2009 and 2007 new and full subsidy notifications of Chile; Cuba; Honduras; Jamaica; Korea; Macao, China; Singapore; Suriname; and Trinidad and Tobago. The Committee also continued the review of certain 2007 new and full subsidy notifications of Argentina; European Union; Japan; and Paraguay.

¹² For further information, see the Report (2009) of the WTO Committee on Subsidies and Countervailing Measures (G/L/906), October 26, 2009.

¹³ The European Union is counted as one Member. These 90 notifications do not include notifications submitted by Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, the Slovak Republic and Slovenia before these Members acceded to the European Communities.

Committee reviewed actions taken by several Members, including Australia, Brazil, Canada, the European Union and the United States.

3. Subsidy Notification by the United States

The United States submitted its subsidy notification in May 2009 consistent with its subsidy notification obligations under the Subsidies Agreement. Researching and assembling the necessary detailed information regarding U.S. assistance programs and consulting extensively with numerous federal and state agencies was a major undertaking requiring a significant commitment of staff and other resources of both USTR and Commerce. The U.S. subsidy notification submitted in 2009 included over 50 federal programs and over 500 state programs notified. This reflected an intensified effort by Commerce and USTR, heightened cooperation between federal and state government personnel and the further institutionalization of the U.S. WTO subsidy notification process.

4. Notification Improvements

During 2009, the Subsidies Committee adopted several changes to the standard format for semi-annual reports of countervailing measures and the minimum information to be provided in connection with the notification of preliminary or final countervailing measures, as required under Article 25.11 of the Subsidies Agreement. In October 2009, the Subsidies Committee adopted changes analogous to those made in the Antidumping Committee, as well as certain proposals made by the United States. The new notification format streamlines and improves the information available in notifications of preliminary and final countervailing actions. The new format will also result in helpful new information being provided, such as the names of programs determined to be countervailing in all CVD proceedings. Members are also now encouraged to submit electronically to the WTO Secretariat copies of the public determinations of countervailing duty actions – even if in a non-WTO language – as attachments to the *ad hoc* notifications of preliminary and final determinations. Overall, the additional information provided will increase transparency as to countervailing duty actions taken and help Members to identify trade-distorting subsidy practices.

In March 2009, the Chairman of the Trade Policy Review Body, acting through the Chairman of the General Council, requested that all committees discuss "ways to improve the timeliness and completeness of notifications and other information flows on trade measures". The United States fully supported this initiative throughout the year and developed proposals that would encourage Members to be more transparent in their industrial subsidy policies. Discussions took place throughout 2009, and consequently, the Committee agreed that a new annex should be included in the Committee's annual report that will provide greater detail regarding the extent to which each Member has or has not met its subsidy notification obligations. Additionally, a new "one-time" notification format was created for Members – largely least developed country Members – that have not established a legal framework and competent authorities to conduct CVD investigations. Lastly, Committee Members agreed to provide all notifications electronically to the Secretariat, which will facilitate and expedite circulation and posting on the WTO website.

5. Article 27.4 Update

Under the Subsidies Agreement, most developing country Members were obligated to eliminate their export subsidies by December 31, 2002. Article 27.4 of the Subsidies Agreement authorizes the Subsidies Committee to extend this deadline where justified. If the Committee does not affirmatively determine that an extension is justified, the export subsidy at issue must be phased out within two years.

To address the concerns of certain small developing country Members, a special procedure within the context of Article 27.4 of the SUBSIDIES Agreement was adopted at the Fourth WTO Ministerial Conference in 2001. Under this procedure, a developing Member meeting all of the agreed-upon qualifications became eligible for annual extensions for a five-year period through 2007, in addition to the two years referred to under Article 27.4. Antigua and Barbuda, Barbados, Belize, Costa Rica, Dominica, the Dominican Republic, El Salvador, Fiji, Grenada, Guatemala, Jamaica, Jordan, Mauritius, Panama, Papua New Guinea, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Uruguay have made yearly requests since 2002 under this special procedure.

Following a request for a further extension, in 2007 the Subsidies Committee decided to recommend to the General Council that it extend the transition period until 2013 under similar special procedures as those that had previously been in place, with a two-year phase-out period ending in 2015. An important outcome of these negotiations, insisted upon by the United States and other developed and developing countries, was that the beneficiaries have no further recourse to extensions beyond 2015. The General Council adopted the recommendation of the Subsidies Committee in July 2007.

Specific export subsidy program extension requests under the new procedures¹⁴ were made in 2009 by all of the developing country Members listed above. These requests required, *inter alia*, a detailed examination of whether the applicable standstill and transparency requirements had been met. In total, the Subsidies Committee conducted a detailed review of more than 40 export subsidy programs. At the end of the process, all of the extension requests were granted. (A chart of all the programs is found in Attachment 3).

6. Permanent Group of Experts

Article 24 of the Subsidies 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 Subsidies 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 Member, a “confidential” advisory

¹⁴ See WT/L/691

opinion on the nature of any subsidy proposed to be introduced or currently maintained by that Member. Article 24 further provides for the Committee to elect the experts to the PGE, with one of the five experts being replaced every year.

In the beginning of 2009, the Permanent Group of Experts had five members: Mr. Asger Petersen (Denmark), Dr. Chang-fa Lo (Chinese Taipei); Dr. Manzoor Ahmad (Pakistan); Mr. Zhang Yuqing (China); and Mr. Jeffrey A. May (United States). Mr. Peterson's term ended in Spring 2009 and the Committee elected Mr. Gerard Depayre (France) to replace him.

7. The Methodology for Annex VII (b) of the Subsidies Agreement

Annex VII of the Subsidies Agreement identifies certain lesser developed country Members that are eligible for particular special and differential treatment. Specifically, the export subsidies of these Members are not prohibited and, therefore, are not actionable as prohibited subsidies under the dispute settlement process. The Members 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, at the time of the negotiation of the Agreement, had a per capita GNP under \$1,000 per annum and that are specifically listed in Annex VII(b).¹⁵ A country automatically "graduates" from Annex VII(b) status when its per capita GNP rises above the \$1,000 threshold. At the WTO's Fourth Ministerial Conference, Ministers made a decision calling for the calculation of the \$1,000 threshold in constant 1990 dollars. The WTO Secretariat updated these calculations, and in 2009 the Dominican Republic and Guatemala both graduated from Annex VII(b) status.¹⁶

8. Prospects for 2010

In 2010, as noted above, the United States will continue to focus on China's subsidy programs, and will consider alternative approaches to bring greater transparency to China industrial policy regime. The Subsidies Committee will continue to work to improve upon Members' notification obligations. Among the proposals that may be addressed further are two issues raised by the United States; namely, the failure of Members to respond to subsidy program questions submitted pursuant to Article 25.8 of the Subsidies Agreement and, the significant lack of notification of sub-central subsidy programs across the Membership. Finally, given the various stimulus packages Members have implemented in response to the financial crisis, it is expected that the Subsidies Committee will remain a forum to discuss the consistency of such programs with Members' obligations under the Subsidies Agreement.

¹⁵ Members identified in Annex VII(b) are: Bolivia, Cameroon, Congo, Cote d'Ivoire, Egypt, Ghana, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka, and Zimbabwe. In recognition of a technical error made in the final compilation of this list and pursuant to a General Council decision, Honduras was formally added to Annex VII(b) on January 20, 2001.

¹⁶ See G/SCM/110/Add.5.6.

G. U.S. Monitoring of Subsidy-Related Commitments

1. WTO Accession Negotiations

Countries and separate customs territories seeking to join the WTO must negotiate the terms of their accession with current Members. In a typical accession negotiation, the applicant submits an application to the WTO General Council, which establishes a Working Party to review information on the applicant's trade regime and to oversee the negotiations. Accession negotiations involve a detailed review of the applicant's entire trade regime by the Working Party and bilateral negotiations for import market access.

The economic and trade information reviewed by the Working Party includes the acceding candidate's subsidies regime. Subsidy-related information is summarized in a memorandum submitted by an applicant detailing its foreign trade regime, which is supplemented and corroborated by independent research throughout the accession negotiation. USTR and Commerce, along with an interagency team, review the compatibility of acceding parties' subsidy regimes with WTO subsidy rules. Specifically, the interagency team examines information on the nature and extent of the candidate's subsidies, with particular emphasis on subsidies that are prohibited under the Subsidies Agreement. Additionally, an accession candidate's trade remedy laws are examined to determine their compatibility with the relevant WTO obligations.

United States' policy is to seek commitments from accession candidates that they eliminate all prohibited subsidies upon joining the WTO, and that they will not introduce any such subsidies in the future. The United States may seek additional commitments regarding any subsidies that are of particular concern to U.S. industries.

Currently, the WTO includes 153 members. In 2009, WTO accession negotiations continued with a wide range of countries that, to varying degrees, included discussion of those countries' subsidies regimes. The countries included Laos, Montenegro, Seychelles and Yemen, among others.

In August 2009, Commerce officials travelled to Vientiane, Lao PDR, to participate in a three-day technical exchange with Lao PDR Government officials in the international trade and economic development policy agencies. These officials are also responsible for the data collection and analysis necessary for preparing a draft subsidy notification for review by the Lao PDR's WTO accession Working Party. Based on the training provided during this exchange, we also expect Lao PDR to intensify its efforts to identify reportable subsidies and to begin the process of rescinding those which must be eliminated as a condition of their accession to the WTO. As a result, Lao PDR officials have formally committed to submitting a draft subsidy notification for the Working Party's review.

2. WTO Trade Policy Reviews

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

By describing Members' subsidy practices, these reviews play an important role in ensuring that WTO Members meet their obligations under the Subsidies Agreement. TPRs also provide a broader context in which to assess a Member's subsidy policies and their role in that Member's economy than do the Subsidies Committee notification reviews. In reviewing these reports, USTR and Commerce focus on the information concerning the subsidy practices detailed in the report, but also conduct additional research on potential omissions regarding known subsidy practices that have not been reported. In 2009, USTR and Commerce reviewed 16 Members' TPRs, including those of Brazil, the EU, Japan and SACU members.¹⁷

CONCLUSION

In 2009, the financial crisis posed significant new challenges to WTO Members who sought to intervene in their economies while remaining consistent with their WTO obligations – most critically, the obligations imposed by the Subsidies Agreement. Initially, WTO Members sought increased transparency for the various measures taken by governments to counteract the economic contraction. The Subsidies Committee played its part in advancing those efforts, even if only incrementally. More broadly, however, the financial crisis led Members to consider carefully the WTO's subsidy rules. Moving forward, a key question for consideration by the Rules Group is whether stronger rules are needed to prevent market and trade distortions potentially caused by the emergency economic policies of others. Or, alternatively, do the existing rules strike the right balance by permitting governments to subsidize so long as they do not adversely affect the interests of others? This will be a key area of focus by the United States in 2010.

The most significant continuing issue for the U.S. subsidy enforcement efforts in 2009 remained China's industrial subsidy policies. The United States will continue to press for a full accounting of China's subsidy measures, especially those measures taken at the sub-central levels of government. In the absence of such an accounting, the United States will intensify its efforts to independently identify subsidy measures in China, focusing

¹⁷ SACU members include Botswana, Lesotho, Namibia, South Africa and Swaziland.

particularly on those measures that may be prohibited. In 2009, the U.S. efforts in this regard not only led to a very significant achievement in ensuring that China adheres to its Subsidy Agreement obligations, but also shed much greater light on the relationship between the central and sub-national levels of government in China with respect to the development and implementation of industrial policy. As a consequence, the United States now has a deeper understanding of the context in which subsidies are provided, as well as the mechanisms by which they are distributed. This knowledge will enhance our efforts going forward in identifying unreported measures, obtaining their elimination and providing a level playing field for American workers and businesses.