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Ms. Gloria Blue
Executive Secretary
Trade Policy Staff Committee
Office of the United States Trade Representative
1724 F Street, N.W.
Washington, DC 20508
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RE: Request for Comments Concerning China's Compliance with its WTO Commitments

Dear Ms. Blue:

In response to a request from the Office of the United States Trade Representative ("USTR"),¹ the American Iron and Steel Institute ("AISI"), on behalf of its U.S. member companies, hereby submits comments to the interagency Trade Policy Staff Committee ("TPSC") regarding China's compliance with the commitments it made upon its accession to the World Trade Organization ("WTO"). Of the categories listed in USTR's request, these comments particularly relate to internal policies affecting trade (*e.g.*, subsidies and taxes levied on exports), intellectual property rights, and other WTO commitments.

Executive Summary

As demonstrated throughout this submission, China's continued failure to comply with its WTO obligations is a major problem, both for American steel producers and for other U.S. manufacturers. Given that it has now been almost a full decade since China joined the WTO, AISI urges the U.S. government to take a more aggressive approach to this issue. The key points in support of AISI's argument are summarized as follows:

¹ See Office of the U.S. Trade Representative, "Request for Comments and Notice of Public Hearing Concerning China's Compliance With WTO Commitments," 74 Fed. Reg. 44895 (Aug. 31, 2009).

- From 2003 to 2008, Chinese crude steel production increased by *280 billion* metric tons ("MT") – a volume three times total crude steel production in the United States. As a result of this increase in production, China has gone from being a net importer of steel to a major net *exporter* of steel. Unfairly-traded steel from China has caused severe harm to American steel producers, and is also causing serious environmental damage.
- There can be no question that China's increased production has been made possible, in large part, by massive government subsidies – many of which are prohibited by WTO rules. The U.S. Department of Commerce ("DOC") has specifically identified numerous subsidies benefiting Chinese steel producers. Furthermore, China not only maintains policies that will lead to further subsidization going forward, but also manipulates its value added tax ("VAT") system to manage and promote exports of its steel products.
- Although China pledged, as part of its WTO accession, that it would not "influence" commercial decisions of its state-owned enterprises, the Chinese government continues to maintain a heavy amount of control over state-owned steel producers.
- China has taken numerous measures to inappropriately aid its producers in securing access to raw materials, and to manipulate raw material prices in a manner that will give Chinese producers an unfair advantage over their U.S. competitors. Indeed, the U.S. government recently filed a WTO case against China on this very issue.
- Despite years of complaints by American manufacturers, China continues to keep the value of its currency at artificially-low levels that give Chinese producers an unfair advantage in the U.S. market. The U.S. government should take far more aggressive action to address this issue.
- Given that China has not fully complied with its WTO obligations, the United States must effectively enforce its trade remedy laws. Among other things, the United States should continue to treat China as a "non-market" economy for purposes of U.S. antidumping laws.
- The U.S. government should also effectively exercise its authority, under the WTO and U.S. law, to impose product-specific safeguards on Chinese imports where appropriate.
- The U.S. government should also seek to change international tax rules that place U.S. companies at an unfair disadvantage vis-à-vis countries like China that rely on a VAT system.

- Pursuant to China's WTO accession, Chinese imports are subject to WTO agreements relating to product safety. The U.S. government should fully exercise its rights under the relevant agreements to keep unsafe Chinese products out of this market.
- The WTO recently adopted a panel report ruling that Chinese law does not adequately provide for the protection and enforcement of intellectual property rights. The U.S. government should follow up with China to ensure that the rulings and recommendations in this report are fully implemented.

In short, the evidence of China's failure to comply with its WTO obligations – and of the need for the United States to aggressively enforce its rights under WTO agreements – is simply overwhelming.

I. China's Non-Compliance With Its WTO Obligations Remains a Severe and Growing Problem for American Steel Producers and Other U.S. Manufacturers

Before turning to specific concerns about China's non-compliance with its WTO commitments, AISI first emphasizes that this non-compliance is having serious, long-term consequences for American steel producers. China acceded to the WTO on December 11, 2001. Less than three years later, in September 2004, AISI supplied the TPSC with detailed comments about China's failure to comply with its WTO commitments.² AISI raised similar concerns in 2005, 2006, 2007, and 2008.³ In each submission, AISI has documented how China has used subsidies and other forms of government support to build an enormous steel industry in violation of market principles and China's WTO commitments.

There can be no doubt that these concerns were justified. Last year, USTR's 2008 Report to Congress on China's WTO Compliance found that "significant questions have arisen regarding China's adherence to ongoing WTO obligations,

² See Letter from Barry D. Solarz, Vice President of AISI, to Gloria Blue, Executive Secretary of the TPSC (Sept. 14, 2004).

³ See Letter from Barry D. Solarz, Vice President of AISI, to Gloria Blue, Executive Secretary of the TPSC (Sept. 6, 2005); Letter from Barry D. Solarz, Vice President of AISI, to Gloria Blue, Executive Secretary of the TPSC (Sept. 18, 2006); Letter from Barry D. Solarz, Vice President of AISI, to Gloria Blue, Executive Secretary of the TPSC (Sept. 14, 2007); Letter from Barry D. Solarz, Vice President of AISI, to Gloria Blue, Executive Secretary of the TPSC (Sept. 22, 2008).

including core WTO principles.”⁴ It also found that “these problems can be traced to China’s pursuit of industrial policies that rely on excessive, trade-distorting government intervention intended to promote or protect China’s domestic industries.”⁵ Moreover, USTR observed that, rather than making progress toward further market liberalization in compliance with its WTO obligations, there is now evidence of a “trend toward a *more restrictive* trade regime” in China.⁶

A. China’s Massive Steel Industry Continues to Grow

Unfortunately, the trend toward a more restrictive trade regime that USTR observed in 2008 continues. Indeed, China’s steel industry continues to grow dramatically due to trade-distorting practices:

- Chinese crude steel production soared from 222 million MT in 2003 to 502 million MT in 2008 – an increase of 280 million MT.⁷ To put these figures in context, consider that in 2008 total crude steel production in the United States was 91 million MT.⁸ In other words, over the last five years, China’s steel production has *increased* by a volume greater than *three* times the *total* production of the U.S. industry.⁹
- China’s growth in steel production has far outpaced Chinese consumption. In 2003, China’s net *imports* of steel were 34.65 million MT.¹⁰ In 2008,

⁴ USTR, 2008 Report to Congress on China’s WTO Compliance (Dec. 2008) (2008 USTR Report) at 3.

⁵ *Id.*

⁶ *Id.* at 4 (emphasis added).

⁷ World Steel Association, “World crude steel production decreases by 1.2% in 2008” (Jan. 22, 2009), *available at* <http://worldsteel.org> (last visited Aug. 13, 2009) at 25.

⁸ *Id.*

⁹ $91 \times 3 = 273 < 280$.

¹⁰ Peter F. Marcus and Karlis M. Kursis, “Core Report ZZZZ: Global Steel Export Pricing Forecast to 2015,” *World Steel Dynamics* (July 2007) (hereinafter “Core Report ZZZZ”) at 23.

China's net *exports* of steel were 49.2 million MT.¹¹ In other words, China's steel trade balance shifted by 83.85 *million MT* over this period¹² – an amount almost equal to total U.S. crude steel production.

- It appears that in 2009 China will again produce far more steel than is justified by Chinese demand. The China Iron and Steel Association (“CISA”) anticipates that China will produce over 500 million MT of crude steel in 2009,¹³ even though Chinese consumption will only be 470 million MT.¹⁴ Indeed, World Steel Dynamics reports that for the next five years “the demand for steel {in China} will not be strong enough to overcome the excess supply in the steel industry.”¹⁵
- China's actions are particularly striking when viewed in light of the current global economic crisis. In the first half of 2009, the U.S. steel industry reduced crude steel production by 51.8 percent compared to the first half of 2008.¹⁶ Similarly, worldwide crude steel production (excluding China) decreased by 35 percent.¹⁷ In contrast, Chinese crude steel production actually *increased* by 1.2 percent.¹⁸ As a result, China's share of global

¹¹ World Steel Association, “World Steel in Figures 2009” (June 30, 2009), available at <http://worldsteel.org> (last visited Aug. 13, 2009) (“World Steel in Figures 2009”).

¹² $34.65 + 49.2 = 83.85$.

¹³ China Iron & Steel Association, “China may produce 500 million tons of steel this year” (Aug. 6, 2009), available at <http://www.chinaisa.org> (last visited Aug. 19, 2009).

¹⁴ CISA, “No new expansion approvals in three years” (Aug. 17, 2009), available at <http://www.chinaisa.org> (last visited Aug. 26, 2009) (“No New Expansions”). It should be noted that China often claims that it will use its control over the steel industry to curb production and reduce excess capacity. *See id.* However, as discussed in Section II.B of this submission, these claims should be rejected.

¹⁵ Liu Jinghai, “Core Report H: Chinese Steel Hits the Great Wall,” *World Steel Dynamics* (May 2009) (“Core Report H”) at 17.

¹⁶ World Steel Association, “June 2009 Crude Steel Production” (July 20, 2009), available at <http://worldsteel.org> (last visited Aug. 13, 2009).

¹⁷ Total worldwide crude steel production (excluding China) fell from 435 million MT in the first half of 2008 to 283 million MT in the first half of 2009. *See id.* $(435 - 283) / 435 = 0.35 = 35\%$.

¹⁸ *Id.*

crude steel production grew from 37.7 percent in the first half of 2008¹⁹ to 48.6 percent in the first half of 2009.²⁰ In other words, China has clearly taken advantage of the global economic crisis to gain market share.

- China continues to build additional capacity. China's Ministry of Industry and Information Technology estimates that China's total crude capacity will reach *660 million MT* by the end of 2009 – a year in which Chinese consumption will only be 470 million MT.²¹ In other words, Chinese capacity will exceed Chinese consumption by a staggering *190 million MT*.²² To put this figure into perspective, consider that in 2008 the United States consumed 97.5 million MT of steel.²³ In other words, by the end of 2009, China will be able to supply all of its own steel consumption and still have enough capacity left over to supply twice the amount of steel that the United States consumes each year.

B. Chinese Steel Continues to Injure the U.S. Steel Industry

Of course, this massive production of steel has had a dramatic impact on American steel producers. Indeed, the United States currently maintains antidumping (“AD”) orders on imports of hot-rolled steel, cut-to-length steel plate, rebar, and steel threaded rod from China. The United States also maintains both AD and countervailing duty (“CVD”) orders on imports of light-walled rectangular pipe, welded standard pipe, welded line pipe, and austenitic stainless pressure pipe from China. Each of these orders rests upon findings by the DOC that Chinese mills engaged in unfair trade and findings by the U.S. International Trade Commission (“ITC”) that Chinese imports caused material injury to the relevant domestic industry. These facts show that unfairly traded Chinese steel has harmed U.S. producers.

While the AD/CVD orders listed above have certainly helped, Chinese imports remain a significant problem for American steel producers. In April 2009, for example, U.S. producers of oil country tubular goods (“OCTG”) were forced to

¹⁹ In the first half of 2008, China produced 263 million MT of the world's total steel production of 698 million MT. $263 / 698 = 0.377 = 37.7\%$.

²⁰ In the first half of 2009, China produced 267 million MT of the world's total steel production of 549 million MT. $267 / 549 = 0.486 = 48.6\%$.

²¹ No New Expansions at 1.

²² $660 - 470 = 190$.

²³ World Steel in Figures 2009 at 16.

seek AD/CVD relief after unfairly traded imports of OCTG from China tripled from 725,027 net tons (“NT”) in 2006 to 2,197,556 NT in 2008.²⁴

C. Chinese Steel Causes Environmental Damage

It seems clear that the massive expansion of the Chinese steel industry is also causing serious environmental damage. In March 2009, the Alliance for American Manufacturing (“AAM”) published a study assessing China’s environmental regulation in its steel industry.²⁵ During the time frame studied, the study found that China’s steel industry accounted for about one-third of the world’s steel production.²⁶ However, during this same period China’s steel industry accounted for 50 percent of the world’s production of carbon dioxide from steelmaking.²⁷ The study also found that making a ton of steel in China also results in nearly *twenty times* greater emissions of particulate matter than in the United States.²⁸

The AAM study attributes China’s dramatically higher emissions of greenhouse gases and particulate matter to a number of factors. First, China’s air and water pollution standards for steel production are substantially less stringent than comparable U.S. standards.²⁹ Second, the Chinese steel industry operates in an environment in which enforcement of existing standards is weak and mills do not adequately monitor their own emissions and discharges.³⁰ Third, the enforcement of China’s environmental regulations is largely decentralized, with the national government relying largely on provincial and local governments that have limited resources and little incentive to enforce environmental standards.³¹ Fourth, Chinese steel companies spend considerably less on pollution control equipment than their

²⁴ ITC, Staff Report *Certain Oil Country Tubular Goods from the People’s Republic of China* (May 18, 2009) (“OCTG Staff Report”) at IV-5.

²⁵ Alliance for American Manufacturing, “An Assessment of Environmental Regulation of the Steel Industry in China” (2009), *available at* <http://www.americanmanufacturing.org> (last visited Aug. 19, 2009) (“Environmental Assessment”).

²⁶ *Id.* at vi.

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.* at vii.

³⁰ *Id.*

³¹ *Id.* at viii.

counterparts in the United States.³² In fact, the study found that “U.S. steel companies outspend their Chinese counterparts by around 80 percent per ton of steel on direct operation and maintenance expenditures to control air and water pollution alone.”³³

The United States is actively considering various measures to reduce its greenhouse gas emissions in response to concerns about climate change. The U.S. steel industry is among the most energy-efficient in the world. Indeed, American steel producers have voluntarily reduced their energy consumption by 33 percent since 1990 and now have the lowest carbon dioxide emissions per ton in the world.³⁴ Yet higher costs as a consequence of climate change legislation could harm the competitiveness of U.S. mills. This, in turn, could lead to “carbon leakage” as production moves from the United States to countries like China.

AISI therefore urges that any domestic climate policy not harm the competitiveness of U.S. producers. To that end, the international trade and investment dimension of climate change should be fully analyzed and effectively addressed. To the extent the United States pursues domestic climate change legislation, such legislation should include provisions that would prevent carbon leakage through increased imports of Chinese and other foreign steel. Nothing in the WTO rules would bar the United States from including such provisions. Indeed, a report prepared this year by the WTO and the United Nations Environmental Program (“UNEP”) recognized that the objective of such provisions is simply “to level the playing field between taxed domestic industries and untaxed foreign competition by ensuring that internal taxes on products are trade neutral.”³⁵ The WTO-UNEP report also found that the WTO rules could permit the inclusion in climate change legislation of provisions that prevent carbon leakage.³⁶

D. Decisive Action Should Be Taken

In short, China’s enormous oversupply of steel is having a disruptive impact on both the United States steel industry and the environment. This oversupply is not

³² *Id.* at ix.

³³ *Id.*

³⁴ AISI, “Climate Policy,” *available at* <http://www.steel.org> (last visited Aug. 26, 2009).

³⁵ *See* WTO-UNEP Report, Trade and Climate Change (2009), *available at* <http://www.wto.org> (last visited Aug. 26, 2009) at xix.

³⁶ *Id.*

the function of any comparative advantage that China possesses for steel production. Instead, it is a direct consequence of China's maintaining specific policies to support an export-driven economy using subsidies and other unfair practices that violate China's WTO commitments.

The U.S. government should take decisive action to address these issues, including the following:

- pursuing additional dispute settlement proceedings at the WTO as necessary to address China's failures to comply with its WTO obligations;
- immediately taking effective steps to counter China's manipulation of its currency (a major subsidy to Chinese producers);
- pursuing bilateral and other consultations, utilizing the leverage of access to the U.S. market as necessary, to obtain true rectification of the market-distorting practices that China has used and continues to use to support its preferred industries;
- ensuring strong and effective enforcement of U.S. trade laws, particularly our AD/CVD laws; and
- pursuing a global steel sectoral approach with respect to climate change regulations and ensuring that any new U.S. legislation relating to climate change includes provisions to prevent carbon leakage from occurring.

II. Issues of Particular Importance to U.S. Steel Producers

This submission does not attempt to identify and discuss every outstanding issue with respect to China's WTO compliance. Instead, it focuses on several issues of core concern that are imperative for the U.S. government to address. The primary issues addressed in this submission can be found in Figure 1. Many of these issues are directly relevant not only to the domestic steel industry, but to all U.S. manufacturers, many of whom are customers of AISI members.

Figure 1: Issues Regarding Key China WTO Commitments

Commitment	Time Frame	Issue
Limit and/or eliminate trade-distorting subsidies (SCM Agreement).	On accession	China continues to provide significant subsidies to its steel producers.
Ensure that the government does not interfere with state-owned enterprises (Report of the Working Party on the Accession of China).	On accession	As shown by its steel policy and orders of the National Development and Reform Commission, China continues to micromanage state-owned enterprises including steel producers.
Dismantle export restrictions (GATT Article XI).	On accession	China continues to impose WTO-inconsistent restrictions on export of key raw materials.
End export subsidies (SCM Agreement Article 3).	On accession	China continues to provide a variety of export subsidies.
Allow other Members to treat China as a non-market economy ("NME") (WTO Protocol on the Accession of China at § 15(a)(ii)).	Agreed to allow NME treatment for 15 years after accession.	The U.S. government should continue to treat China as an NME and should reject the notion that China's NME status limits the application of U.S. CVD laws to subsidized goods from China.
Permit imposition of product-specific safeguards against Chinese imports where necessary and appropriate (WTO Protocol on the Accession of China at § 16).	Agreed to allow special rules for 12 years after accession	The U.S. government should ensure that product-specific safeguards serve as a viable remedy.
Implement neutral and transparent application of tax laws (GATT Article III).	On accession	China continues to manipulate its VAT system to benefit Chinese companies.
Enforce intellectual property laws (WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS)).	On accession	While the WTO recently adopted a ruling favorable to the United States in a case regarding intellectual property rights, the United States must follow up to ensure that China properly implements the ruling.

A. Subsidies

Upon its accession to the WTO, China assumed the obligations of the WTO Agreement on Subsidies and Countervailing Measures (“SCM Agreement”).³⁷ In particular, China committed that by the time of its accession it would eliminate all subsidies prohibited under Article 3 of the SCM Agreement.³⁸ China also agreed that other WTO members could apply CVD orders against Chinese imports consistent with the SCM Agreement and could address prohibited and actionable subsidies through WTO litigation.³⁹

Notwithstanding these commitments, Chinese manufacturers – including Chinese steel producers – continue to benefit from massive government subsidies. The evidence on this point is overwhelming.⁴⁰ In its most recent report, issued in November 2008, the U.S.-China Economic and Security Review Commission (“USCC”) stated that “China continues to provide favored domestic companies and industries with additional government subsidies, including favorable tax treatment; low-interest loans and loan forgiveness; discounted land and electrical power; lax

³⁷ WTO Working Party on the Accession of China, *Report of the Working Party on the Accession of China*, WT/ACC/CHN/49 (Oct. 1, 2001) available at <http://www.uschina.org> (last visited Aug. 20, 2009) (hereinafter “Working Party Report”) at ¶¶ 166-68, 171, 174; see also World Trade Organization, *Protocol on the Accession of the People’s Republic of China*, WT/L/432 (Nov. 10, 2001) (hereinafter “China Protocol of Accession”) at ¶ 10.3.

³⁸ Working Party Report at ¶¶ 166-68, 171, 174; China Protocol of Accession at ¶ 10.3; see also Agreement on Subsidies and Countervailing Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, Legal Instruments—Results of the Uruguay Round, 33 I.L.M. 1125 (1994).

³⁹ China Protocol of Accession at ¶ 15.

⁴⁰ Unfortunately, China’s failure to comply with its WTO obligations makes it impossible to measure precisely the scope of this support. Pursuant to Article XVI of the General Agreement on Tariffs and Trade (“GATT”) and Article 25 of the SCM Agreement, China is required to notify members of its subsidy programs every year. In fact, China did not submit any such notification until April 2006, over four years after it acceded to the WTO. USTR 2008 Report at 42. Furthermore, as USTR has recognized, this notification was woefully incomplete. *Id.* Despite USTR repeatedly expressing concern over this issue, China has not provided any further subsidies notifications to the WTO – a failure that represents yet another violation of its WTO obligations.

enforcement of pollution control regulations; and deliberate market-entry barriers.”⁴¹ Similarly, USTR’s 2008 report on China’s WTO compliance states that “China continues to provide injurious subsidies to its domestic industries, and some of these subsidies appear to be prohibited under WTO rules.”⁴²

Furthermore, the United States initiated a WTO case against China in December 2008 challenging an industrial policy that promotes sales of “famous brands” of Chinese merchandise.⁴³ The policy is designed to promote the development of global Chinese brand names and to increase sales of Chinese-branded merchandise around the world.⁴⁴ The United States stated that it was initiating the case “not only because these programs appear to incorporate export subsidies (which are generally prohibited by applicable WTO rules), but also because of the protectionist industrial policy apparently underlying these programs.”⁴⁵

1. *Additional Evidence of Subsidies Has Come to Light*

During 2009, further evidence of Chinese steel subsidies has come to light. While this submission will not recount all such evidence, the following examples more than demonstrate the point:

- The U.S. Department of Commerce (“DOC”) has issued decisions in two CVD investigations involving welded line pipe and austenitic stainless pressure pipe from China.⁴⁶ In those investigations, the DOC specifically

⁴¹ U.S.-China Economic and Security Review Commission, *2008 Report to Congress* (Nov. 2008), available at <http://www.uscc.gov> (last visited Aug. 13, 2009) (hereinafter “USCC 2008 Report”) at 43.

⁴² 2008 USTR Report at 1.

⁴³ See USTR, “United States Files WTO Case Against China Over Illegal Support for Chinese ‘Famous Brands’” (Dec. 18, 2008), available at <http://www.ustr.gov> (last visited Aug. 18, 2009).

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Circular Welded Carbon Quality Steel Line Pipe*, Final Affirmative Countervailing Duty Determination, 73 Fed. Reg. 70961 (Dep’t of Commerce Nov. 24, 2008); *Circular Welded Austenitic Stainless Pressure Pipe*, Final Affirmative Countervailing Duty Determination, 74 Fed. Reg. 4936 (Dep’t of Commerce Jan. 28, 2009).

identified numerous subsidies benefiting Chinese companies, including the following:

- provision of land for less than adequate remuneration;⁴⁷
- provision of hot-rolled steel for less than adequate remuneration;⁴⁸
- provision of stainless steel coil for less than adequate remuneration;⁴⁹
- export interest subsidies;⁵⁰
- loans contingent upon exporting;⁵¹
- exemption from or reduction in income taxes for certain foreign invested enterprises;⁵²
- direct transfers of funds from the government in the form of grants, refunds of value-added tax (“VAT”), loan interest subsidies, and exemptions from certain fees;⁵³
- income tax credits on purchases of domestically-produced equipment by domestically owned companies;⁵⁴
- preferential lending to state-owned enterprises and the steel industry by state-owned and controlled banks;⁵⁵

⁴⁷ Issues and Decision Memorandum, *Circular Welded Carbon Quality Steel Line Pipe Id.* at 13-18.

⁴⁸ *Id.* at 18-20.

⁴⁹ Issues and Decision Memorandum, *Circular Welded Austenitic Stainless Pressure Pipe* at 16

⁵⁰ Issues and Decision Memorandum, *Circular Welded Carbon Quality Steel Line Pipe* at 22-23.

⁵¹ *Id.* at 23-24.

⁵² *Id.* at 12-13;

⁵³ *Id.* at 20-21, 24-25.

⁵⁴ *Id.* at 25-26.

⁵⁵ *Id.* at 26-27.

- exemption from or reduction in income taxes for companies located in certain development zones;⁵⁶
 - exemption from or reduction in income taxes for certain town and village enterprises;⁵⁷
 - exemption from payment of VAT and tariffs on imported equipment used in production;⁵⁸
- In April 2009, U.S. producers of OCTG brought petitions for AD and CVD relief from imports of OCTG from China. The CVD petition documents a significant number of subsidies provided to Chinese OCTG producers, including: preferential loans, debt-to-equity swaps, equity infusions, loan forgiveness, income tax benefit programs, exemptions from and rebates of VAT, land grants and discounts, the provision of various inputs for less than adequate remuneration, grant programs, subsidies to companies located in certain economic development zones, and subsidies for certain foreign-invested enterprises.⁵⁹
- The European Confederation of Iron and Steel Industries (“EUROFER”) issued a report documenting certain specific types of subsidies provided to the Chinese steel industry.⁶⁰ EUROFER’s analysis was limited to publicly available financial statements of steel companies listed in the Shanghai and Shenzhen Stock Exchanges. Nonetheless, for the period between 2001 and 2007, EUROFER was able to identify the receipt of 3.4 billion Chinese renminbi (“RMB”) (\$420 million) in subsidies to support domestic equipment purchases between 2001 and 2007.⁶¹ The report also identified the receipt of 7.607 billion RMB (\$940 million) in discretionary tax breaks,

⁵⁶ Issues and Decision Memorandum, *Circular Welded Austenitic Stainless Pressure Pipe* at 8.

⁵⁷ *Id.*

⁵⁸ *Id.* at 23.

⁵⁹ See OCTG Petition at Vol. III, pp. 23-140.

⁶⁰ Markus Taube and Christian Schmidkonz, *The State-Business Nexus in China’s Steel Industry—Chinese Market Distortion in Domestic and International Perspective*, (January 2009) prepared for EUROFER (“EUROFER Report”).

⁶¹ *Id.* at 132. The average exchange rate between 2001 and 2007 was 8.1 RMB per U.S. dollar. See Oanda, “FXAverage - Historical Currency Averages,” available at <http://www.oanda.com/convert/fxaverage>.

753 million RMB (\$93 million) in preferential lending facilities, and 2.151 billion RMB (\$260 million) in various other subsidies between 2002 and the first quarter of 2008.⁶²

-- In June 2009, the USCC released a study that assessed the subsidies provided to China's designated "strategic and heavyweight industries," including steel.⁶³ The study included the following key findings:

- A case study of Angang Steel Co Ltd., China's second largest steel producer by market value, shows that the company received 723 million RMB (\$95 million) in government subsidies in the year 2007 alone.⁶⁴
- These subsidies are harming U.S. steel producers. In fact, the study found that if China stopped providing subsidies to its steel industry, the U.S. steel industry would make an additional \$1.55 billion each year in domestic sales alone.⁶⁵
- The subsidies are also harming the United States economy as a whole. Indeed, for the eleven U.S. industries examined in the report, eliminating Chinese subsidies would increase domestic sales of those industries by approximately \$81 billion, raise worker earnings by \$31 billion, and expand U.S. exports by \$7.6 billion.⁶⁶

-- AISI and the Steel Manufacturers Association ("SMA") have issued a series of papers discussing the subsidies provided to the Chinese steel industry,

⁶² EUROFER Report at 155. The average exchange rate between 2002 and the first quarter of 2008 was 8.1 RMB per U.S. dollar. See Oanda, "FXAverage - Historical Currency Averages," available at <http://www.oanda.com/convert/fxaverage>.

⁶³ USCC, "An Assessment of China's Subsidies to Strategic and Heavyweight Industries" (June 23, 2009), available at <http://www.uscc.gov> (last visited Aug. 18, 2009).

⁶⁴ *Id.* at 78-79. The average exchange rate in 2007 was 7.6 RMB per U.S. dollar. See Oanda, "FXAverage - Historical Currency Averages," available at <http://www.oanda.com/convert/fxaverage>.

⁶⁵ *Id.* at ix, 115.

⁶⁶ *Id.* at 107-108. The eleven industries studied were electricity, energy, petrochemicals, transportation, communications, machinery, automobile, electronics, construction, steel, and aluminum. *Id.*

including a study issued this year examining the U.S.-China economic relationship from the perspective of the domestic steel industry.⁶⁷ These studies have identified over RMB 393 billion (\$52 billion) in subsidies granted to Chinese steel producers.⁶⁸

2. *China's Steel Policy Ensures Continued Subsidization*

It is clear that China will continue subsidizing steel production. China's steel industry is governed by the Steel and Iron Industry Development Policy ("Steel Policy"), which was issued by China's National Development and Reform Commission ("NDRC") in July 2005. The Steel Policy specifically provides for government support in the form of "taxation, interest subsidy, and scientific research funds" for major iron and steel projects utilizing newly developed domestic equipment.⁶⁹ The Steel Policy also states that enterprises need only provide "40% or above" of necessary investment capital for new projects of iron making, steel making and steel rolling, suggesting that the remainder of such capital will be supplied by government funds.⁷⁰ As the USTR recognized last year:

This high degree of government direction and decision-making regarding the allocation of resources into and out of China's steel industry raises concerns not only because of the commitment that China made in its WTO accession agreement that the government would not influence, directly or indirectly, commercial decisions on the part of state-owned or state invested enterprises, but also more generally because it represents another significant example of China reverting to a reliance on government management of market outcomes instead of moving toward a reliance on market mechanisms.⁷¹

⁶⁷ AISI & SMA, "Rebalancing the U.S.-China Economic Relationship: A Steel Industry Perspective" (July 2009), *available at* <http://www.steel.org> (last visited Aug. 19, 2009)

⁶⁸ *Id.* at 10-11; *Money for Metal: A Detailed Examination of Chinese Government Subsidies to its Steel Industry* (July 2007) at iii.

⁶⁹ NDRC, "Steel Industry Development Policy" (July 20, 2005) at Article 16 (English translation).

⁷⁰ *Id.* at Article 23.

⁷¹ 2008 USTR Report at 61.

Unfortunately, the principles of the Steel Policy were reinforced this year with the *Law of the People's Republic of China on the State-Owned Assets of Enterprises*, which became effective May 1, 2009.⁷² This new law is “formulated for the purposes of safeguarding the basic economic system of China, consolidating and developing the state-owned economy, . . . and promoting the development of the socialist market economy.”⁷³ It provides for China to “take measures to promote the centralization of state-owned capital to the important industries and key fields that have bearings on the national economic lifeline and state security.”⁷⁴ Steel is one of the “key” industries favored by the Chinese government for preferential treatment.⁷⁵ To achieve its goals, the new law authorizes China’s State Council, among other things, to remove and appoint directors and senior managers and restructure and transfer assets between state-invested enterprises in the “key” industries.⁷⁶

3. VAT Export Rebates to Manage and Promote Exports

China also manipulates its VAT system to manage and promote exports of its steel products. As USTR recognized in its 2008 report, China eliminated VAT export rebates on some, but not all, steel products over the course of 2007 and 2008.⁷⁷ As a result, “Chinese steel producers shifted their production to value-added steel products for which full or partial VAT export rebates were still available, . . . causing a surge in exports of these products – many of which ended up in the U.S. market.”⁷⁸ For example, one of the products for which VAT export rebates were still

⁷² Law of the People’s Republic of China on the State-Owned Assets of Enterprises, Order of the President of the People’s Republic of China, *available at* <http://www.lawinfochina.com> (last visited Aug. 17, 2009) (“SOAE Law”).

⁷³ *Id.* at Art. 1.

⁷⁴ *Id.* at Art. 7.

⁷⁵ See China National Development and Reform Commission, *Decree No. 41: Directory Catalogue on Readjustment of Industrial Structure* (Mar. 2, 2005); *Catalogue of Major Industries, Products, and Technologies Encouraged for Development in China* at Art. 14 (Dec. 31, 1997), *available at* <http://english.mofcom.gov.cn> (last visited Aug. 28, 2009).

⁷⁶ SOAE Law at Art. 23, 40, 53.

⁷⁷ 2008 USTR Report at 37.

⁷⁸ *Id.*

available was OCTG.⁷⁹ As previously discussed, imports of OCTG from China tripled from 725,027 NT in 2006 to 2,197,556 NT in 2008.⁸⁰

These practices continued in 2009. On April 1, 2009, China raised the export rebates from 5 percent to 13 percent for certain stainless steel and cold-rolled steel products.⁸¹ In addition, on June 1, 2009, China raised export rebates to 9 percent for certain alloy steel, profiled shapes, and structural steel.⁸² CISA vice general secretary Qi Xiangdong stated that the June increase “will encourage bigger mills to export more steel products.”⁸³ Moreover CISA has estimated that “*the move {will} produce \$170 million worth of benefits* for the steel industry this year.”⁸⁴

It should also be noted that the EUROFER report found evidence that China also manipulates exports by adjusting the *timing* of VAT rebates – *i.e.*, by providing rebates instantly or with delay.⁸⁵ More troubling, it also found that, in some instances, China has provided rebates in excess of the VAT payments made by companies.⁸⁶ Such evidence suggests that China is effectively using VAT rebates to provide outright grants to steel producers that are contingent on their exporting steel.⁸⁷

4. Conclusion

Given that China has subsidized its steel industry for years, and that its government policy plainly provides for further subsidies going forward, it is clear that dialogue alone will not be sufficient to solve this problem. Among other things, the U.S. government should aggressively enforce U.S. CVD laws against subsidized imports from China. In particular, the Administration should find that where China manipulates VAT rebates to provide a specific benefit to exporters of merchandise,

⁷⁹ *Id.*

⁸⁰ OCTG Staff Report at IV-5.

⁸¹ Core Report H at 28.

⁸² CISA, “China raises export rebates on steel” (June 1, 2009), *available at* <http://www.chinaisa.org> (last visited Aug. 19, 2009).

⁸³ *Id.* (emphasis added)

⁸⁴ *Id.*

⁸⁵ EUROFER Report at 142.

⁸⁶ *Id.*

⁸⁷ *Id.*

that benefit is countervailable as a subsidy. Moreover, because these rebates are contingent on export, the Administration should treat them as prohibited export subsidies under WTO rules. In addition, the U.S. government should not only aggressively pursue the WTO case that the United States has brought with respect to China's "famous brands" program, it should also continue to pursue additional WTO litigation against Chinese subsidies where appropriate.

B. State-Owned Enterprises

During the course of its accession to the WTO, the Government of China committed that it "would not influence, directly or indirectly, commercial decisions on the part of state-owned enterprises" ("SOEs").⁸⁸ This commitment is particularly significant in the steel context. The EUROFER report found that the Chinese steel industry is "firmly embedded in a powerful state-business nexus" and maintains "very close relations to government agencies on local, provincial as well as central levels."⁸⁹ Indeed, an analysis of the Chinese industry prepared for AISI in 2007 estimated that *91 percent* of Chinese steel production is state-owned or controlled.⁹⁰

Unfortunately, China has not fulfilled its commitment to refrain from influencing decisions of Chinese SOEs. Rather, as discussed in more detail below, there can be no doubt that China continues to maintain a significant degree of "influence" over its steel-producing SOEs. China's 2005 Steel Policy provides detailed guidance for all Chinese steel producers – including SOEs – with respect to many key decisions. In particular, the Steel Policy:

- calls for the reorganization of China's steel industry so that the ten largest Chinese steel producers will account for more than 50 percent of all Chinese production by 2010, and more than 70 percent of all Chinese production by 2020;⁹¹
- mandates that "steel investment projects shall be reported to the National Development and Reform Commission according to application regulations for review and approval;"⁹²

⁸⁸ Working Party Report at ¶ 46.

⁸⁹ EUROFER Report at 10.

⁹⁰ *Money for Metal: A Detailed Examination of Chinese Government Subsidies to its Steel Industry* (July 2007) at 10.

⁹¹ Steel Policy at Article 3.

⁹² *Id.* at Article 22.

- directs that “large-scale steel enterprises shall be mainly arranged in coastal areas;”⁹³
- provides detailed guidance regarding the size of new steel plants,⁹⁴ the minimum size of blast furnaces to be installed in such plants,⁹⁵ and the amount of water and energy to be consumed in such plants;⁹⁶
- stipulates that as a matter of principle, non-Chinese companies are prohibited from controlling Chinese steel producers.⁹⁷

Indeed, as USTR recognized last year, China’s national steel policy is “striking because of the extent to which it attempts to dictate industry outcomes and *involves the government in making decisions that should be made by the marketplace.*”⁹⁸

China often defends its control over the steel industry on the basis that it will use this control to curb production and reduce overcapacity.⁹⁹ But this defense of China’s control over its steel industry is not persuasive:

- First, this government interference is a clear violation of China’s commitment that it “would not influence, directly or indirectly, commercial decisions on the part of state-owned enterprises.”¹⁰⁰ As AISI and other steel producers’ associations from around the world emphasized in comments submitted to

⁹³ *Id.* at Article 11.

⁹⁴ *Id.* at Article 12 (providing that new steel projects in coastal deepwater port areas shall have a capacity of more than 8 million MT).

⁹⁵ *Id.* (providing that the blast furnaces for new steel projects in coastal deepwater port areas shall be over 3,000 cubic meters).

⁹⁶ *Id.* (setting strict targets for water and energy consumption).

⁹⁷ *Id.* at Article 23.

⁹⁸ 2008 USTR Report at 61.

⁹⁹ For example, China’s Ministry of Industry and Information Technology (“MIIT”) declared in August 2009 that “{n}o new steel expansion should be encouraged for the next three years” in order to “curb excessive capacity.” See No New Expansions at 1. MIIT also reaffirmed China’s commitment to eliminate 50 million MT of outdated steel capacity by 2010 through mergers and consolidations. Id.

¹⁰⁰ Working Party Report at ¶ 46.

MIIT in April 2009, these necessary changes to China's steel industry should be driven by market forces – not the Chinese government.¹⁰¹

- Second, because of conflicts between the national government and the local governments in China, it is unclear whether China will be able to eliminate outdated capacity through forced mergers and consolidations.¹⁰² This July, for example, the Jilin provincial government prevented a proposed merger between Tonghua Steel and Beijing-based Jianlong Group after Tonghua Steel workers killed their general manager during protests at the factory.¹⁰³ The general manager had told the workers that he planned to cut the number of local employees from 13,000 to 5,000.¹⁰⁴ In the following month, the Henan provincial government halted a proposed merger between Linzhou Steel and Fenbao Steel after workers protested. The provincial government also ordered production at Linzhou to resume as soon as possible.¹⁰⁵
- Third, the EUROFER report determined that government interference at the national and local levels is causing “irrational capacity expansion and the creation of massive overcapacities.”¹⁰⁶ The national government is encouraging the growth of national champions while at the same time local governments are promoting and protecting their local steel producers.¹⁰⁷

In short, there can be no doubt that China's steel-producing SOEs – which account for most of the production in the world's largest steel industry – are operating in accord with bureaucratic policies, *not* market principles. This outcome represents not only a clear violation of China's WTO commitments, but a significant

¹⁰¹ See Letter from AISI, EUROFER, SMA, Canadian Steel producers Association, Committee on Pipe and Tube Imports, Latin American Steel Producers Association, Mexican Steel Producers Association, and Specialty Steel Industry of North America to Government of China, Ministry of Industry and Information Technology (April 15, 2009), *available at* <http://www.steel.org> (last visited Aug. 26, 2009).

¹⁰² See EUROFER Report at 11.

¹⁰³ China Daily, “Workers speak of Tonghua boss’ murder” (July 31, 2009), *available at* <http://www.chinadaily.cn> (last visited Aug. 18, 2009).

¹⁰⁴ *Id.*

¹⁰⁵ CRU Steel, “Mill takeover halted by workers’ protest in China” (Aug. 18, 2009).

¹⁰⁶ *Id.* at 12, 49-51.

¹⁰⁷ *Id.*

distorting force in steel markets around the world. USTR should take all possible steps – including WTO litigation as appropriate – to encourage China to comply with its WTO commitments regarding SOEs.

C. Raw Materials

In response to the Chinese steel industry's increasing demand for raw materials, China has taken numerous measures to inappropriately aid its producers in securing access to raw materials, and to manipulate raw material prices in a manner that will give Chinese producers unfair advantages over their U.S. competitors. These measures include imposing restraints on the export of raw materials and using public resources to assist Chinese steel producers in acquiring raw materials overseas.

1. Export Restraints

Article XI of the GATT 1994 generally prohibits WTO members from maintaining export restrictions (other than duties, taxes, or other charges), although certain limited exceptions are allowed.¹⁰⁸ China also agreed as part of its WTO accession to eliminate all taxes and charges on exports other than those included in Annex 6 to the Protocol of Accession or applied in conformity with Article VIII of GATT 1994.¹⁰⁹

The evidence is overwhelming that China has not complied with these commitments. In fact, in June 2009, the United States filed a request for consultations at the WTO regarding China's export restraints on numerous raw materials.¹¹⁰ These raw materials – important to the production of steel, aluminum, and other chemicals – include bauxite, coke, fluorspar, magnesium, manganese,

¹⁰⁸ *Id.*

¹⁰⁹ *Id.* Article VIII only permits fees and charges limited to the approximate cost of services rendered and makes clear that any such fees and charges shall not represent an indirect protection to domestic products or a taxation of exports for fiscal purposes. *Id.* This article is not relevant for the present discussion.

¹¹⁰ USTR, "United States Files WTO Case Against China Over Export Restraints on Raw Materials" (June 23, 2009), *available at* <http://www.ustr.gov> (last visited Aug. 18, 2009) ("USTR Raw Materials Press Release"); *see also* Request for Consultations by the United States, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/1 (June 23, 2009) ("China –Raw Materials Request") at 1.

silicon metal, silicon carbide, yellow phosphorus, and zinc.¹¹¹ According to USTR, China imposes several different export restraints on these materials, including export quotas (caps on the volume of the material that may be exported), which are generally prohibited by applicable WTO rules; export duties which China expressly agreed to eliminate when it joined the WTO; and other export related administrative measures and costs, all of which are inconsistent with WTO rules.¹¹² As USTR has recognized, these export restraints can seriously disadvantage downstream producers in the United States and other countries:

First, these restraints limit exporters' access to these raw materials. Second, the restraints can significantly raise the world market prices for the materials, while lowering the prices that domestic Chinese producers have to pay. Lower-priced downstream Chinese products derived from the materials can then enjoy an anticompetitive price advantage vis-à-vis the same products produced outside China.¹¹³

Consider, for example, export restraints with regard to coke, a key input for steel producers. China's Steel Policy specifically states that exports of coke must be restricted.¹¹⁴ Consistent with this policy, China limited coke exports in 2007 to 14 million MT per year and imposed a 15 percent duty on coke exports.¹¹⁵ The 14 million MT quota represented a tiny fraction of China's total coke output of 328 million MT that year.¹¹⁶ By 2009, China had raised the export tax on coke to 40 percent¹¹⁷ and reduced the export quota even further to 11.91 million MT.¹¹⁸ These actions have pushed up export prices for Chinese coke (and the world market price for coke) while keeping down the domestic price of coke paid by Chinese producers.¹¹⁹ For example, in May 2009, the Chinese domestic price for coke was

¹¹¹ *Id.*; China –Raw Materials Request at 1.

¹¹² *Id.*

¹¹³ *Id.*

¹¹⁴ Steel Policy at Article 30.

¹¹⁵ EUROFER Report at 32.

¹¹⁶ *Id.*

¹¹⁷ SBB Analytics China, "China raises coke export tax to 40%" (Aug. 19, 2008).

¹¹⁸ *Id.*

¹¹⁹ See American Scrap Coalition, "Raw Deal: How Governmental Trade Barriers and Subsidies Are Distorting Global Trade in Raw Materials (2008), available at

approximately \$205 per MT,¹²⁰ less than half the Chinese export price for coke of \$450 per MT,¹²¹ which is considered the “world benchmark.”¹²²

These actions by China mandate that the Administration vigorously pursue the case that it has initiated at the WTO regarding China’s export restraints on raw materials. In addition, the Administration should find that these export restraints constitute countervailable subsidies that confer a financial benefit to Chinese producers by allowing them to purchase inputs at less than adequate remuneration.

2. Raw Materials Purchases

In addition to imposing export restraints, China has an established policy of assisting its steel producers in making major acquisitions of raw materials across the world. Indeed, a study conducted by the American Scrap Coalition (“ASC”) in 2008 documents such assistance being provided in the form of “direct subsidies to Chinese enterprises investing overseas, funding of SOEs to obtain raw materials, backing from China’s sovereign wealth fund, support from state-owned policy banks, and intervening in negotiations relating to long-term contracts for iron ore and other raw materials.”¹²³

China has continued providing this assistance to its steel producers in 2009. In March 2009, for example, the Chinese government provided steel producer Maanshan Iron & Steel with a grant of 30 million RMB (\$4.4 million) to finance its share of the Wheelarra iron ore project in Australia.¹²⁴ In August, Fortescue Metals Group Ltd. (“FMG”), Australia’s third largest iron ore supplier, agreed to a 35-percent

<http://www.scrapemergency.com> (last visited Aug. 18, 2009) (“Raw Deal”) at 11.

¹²⁰ CRU Steel, “Uncertainties to keep Chinese steel prices at low levels” (May 19, 2009).

¹²¹ American Metal Market, “China ‘virtually’ stops coke exports to India” (May 4, 2009).

¹²² Resource Net, “Updated View on the Global Coke & Anthracite Markets” (Mar. 2009), available at <http://www.resource-net.com> (last visited Sept. 3, 2009).

¹²³ *Id.* at 21-22.

¹²⁴ SBB Analytics China (Mar. 9, 2009) at 2.

price cut for iron ore fines as part of a supply deal with China's Baosteel Group.¹²⁵ The deal was conditioned on \$6 billion in financing being provided to FMG – part of which will come through sovereign wealth fund China Investment Corporation.¹²⁶ In a more dramatic intervention, China arrested four employees of Australian iron-ore supplier Rio Tinto in August after a breakdown in negotiations between CISA and Rio Tinto over the benchmark price for iron ore.¹²⁷ As one analyst described the incident:

{T}he arrests are part of a bigger picture that reflects the true economics of doing business in China – with the ultimate {Chinese} customer not only able to wield its clout through its purchasing power or diplomatic moves, but {also through} the ability to detain employees if they sense a losing hand.¹²⁸

Like the export restraints it has imposed on raw materials, this assistance by the Chinese government is designed primarily to advantage China's domestic manufacturers and to enhance downstream exporting industries. However, such interference has adversely impacted the availability and price of critical raw materials globally, increasing input costs for manufacturers in other markets, including the United States. Accordingly, the Administration should aggressively press China to cease this practice. It should also find that, where China provides assistance to certain enterprises or industries to acquire raw materials overseas, any benefit received by the enterprises or industries is countervailable as a subsidy.

D. Currency Manipulation

AISI members, along with other U.S. manufacturers, have long expressed concern over China's policy of controlling the exchange rate between its currency (known as the renminbi or the yuan) and the U.S. dollar. In 2004, for example, AISI joined a coalition of U.S. industrial, service, agricultural, and labor associations

¹²⁵ "Another twist in China iron ore negotiations" (Aug. 17, 2009), available at <http://www.mineweb.com> (last visited Aug. 30, 2009); American Metal Market, "Iron ore deal unlikely to end China's price problems" (Aug. 17, 2009).

¹²⁶ *Id.*

¹²⁷ American Metal Market, "China's bullying behavior backfires with a global bang" (Aug. 1, 2009); Wall Street Journal, "Rio Tinto Arrests Throw Firms Off Balance" (Aug. 13, 2009), available at <http://www.wsj.com> (last visited Aug. 30, 2009).

¹²⁸ *Id.*

seeking relief under Section 301(a) of the Trade Act of 1974, as amended,¹²⁹ from China's manipulation of the renminbi.¹³⁰ As the Section 301 petition demonstrated, China's exchange-rate policy constitutes an export subsidy within the meaning of Articles 1, 2, and 3 of the WTO Subsidies Agreement, and GATT Articles VI and XVI.¹³¹ The reasoning behind this conclusion was recently summarized by the USCC as follows:

In simple terms, maintaining a low value for the RMB means that Chinese exports will be cheaper than they would be if the price of the currency were determined by market forces. The result is that Chinese goods are cheaper in the United States, and U.S. exports are more expensive in China, which provides China with an effective export subsidy and an incentive for U.S. companies to move their production to China. This problem also confronts U.S. exporters in other markets where they compete against Chinese products.¹³²

The U.S. government rejected the 2004 petition for Section 301 relief, and has consistently refused to pursue WTO litigation against China regarding this matter. Instead, it has sought to address concerns about currency manipulation through dialogue with the Chinese government. Unfortunately, these efforts have not been successful.

In 2005, China announced that it would allow more flexibility in its exchange rate. At the time, estimates placed the value of the renminbi at up to 40 percent below what its value would have been absent government intervention.¹³³ After China's announcement, the RMB appreciated from 8.28 RMB per dollar to 6.81 RMB per dollar in July 2008,¹³⁴ an adjustment of only 17.8 percent.¹³⁵ Starting in

¹²⁹ 19 U.S.C. §§ 2411 *et seq.* (2000).

¹³⁰ Petition for Relief under Section 301(a) of the Trade Act of 1974 on behalf of the China Currency Coalition (Sept. 9, 2004), *available at* <http://www.chinacurrencycoalition.org> (last visited Sept. 6, 2008).

¹³¹ *Id.* at 50.

¹³² USCC 2008 Report at 27.

¹³³ Congressional Research Service Report for Congress, "China's Currency: Brief Overview of U.S. Options" at CRS-2 (Nov. 29, 2005) (available at <http://fpc.state.gov/documents/organization/57797.pdf>).

¹³⁴ *See* Federal Reserve Statistical Release: Foreign Exchange Rates (Daily), available at <http://www.federalreserve.gov> (last visited Aug. 19, 2009).

July 2008, however, China halted the appreciation of the RMB “due to the Chinese government’s fear that a strong RMB will damage China’s exports.”¹³⁶ In fact, the value of the RMB currently stands at 6.83 RMB per dollar.¹³⁷ Even an economist at a Chinese state think-tank has conceded that “{w}e have now moved back to a virtual US dollar peg.”¹³⁸ Given the dollar’s “extreme gyrations” against other currencies since July 2008, the fact that RMB-dollar exchange rate has remained steady “can only have been done with an active Chinese decision to tie itself to the dollar.”¹³⁹ Indeed, a recent econometric study indicates that China’s currency still remains undervalued by 40 percent against the dollar.¹⁴⁰

In short, there is overwhelming evidence that China is manipulating its currency. As the USCC concluded in its 2008 report, “currency manipulation has been a useful tool in supercharging China’s export machine.”¹⁴¹ In January 2009, in written testimony provided to the Senate Finance Committee as part of his confirmation hearings, Treasury Secretary Timothy Geithner stated that “President Obama – backed by the conclusions of a broad range of economists – believes that *China is manipulating its currency.*”¹⁴² He added that President Obama pledged “to use aggressively all the diplomatic avenues open to him to seek change in China’s currency practices.”¹⁴³

¹³⁵ $8.28 - 6.81 = 1.47$; $1.47 / 8.28 = 0.178 = 17.8$ percent.

¹³⁶ USCC 2008 Report at 42.

¹³⁷ See Federal Reserve Statistical Release: Foreign Exchange Rates (Daily), available at <http://www.federalreserve.gov> (last visited Aug. 19, 2009).

¹³⁸ Financial Times, “China’s forex reserves pass \$2,000 bn” (July 15, 2009), available at <http://www.ft.com> (last visited Aug. 19, 2009)..

¹³⁹ Michael Hennigan, “China has pegged currency to US dollar since July 2008 to help exporters” (July 1, 2009), available at <http://www.finfacts.ie> (last visited Aug. 26, 2009).

¹⁴⁰ Peterson Institute for International Economics, “2009 Estimates of Fundamental Equilibrium Exchange Rates” (June 2009), available at <http://www.iie.com> (last visited Aug. 26, 2009).

¹⁴¹ USCC 2008 Report at 27.

¹⁴² *Answers to Finance Committee Questions for the Record*, Hearing on Confirmation of Mr. Timothy F. Geithner to be Secretary of the U.S. Department of Treasury January 21, 2009 at 81.

¹⁴³ *Id.*

Remarkably, despite this testimony, the Administration has refused to cite China as a currency manipulator. Specifically, in a semiannual report to Congress on the currency practices of key trading partners, Treasury Secretary Geithner stated that “Treasury did not find that any major trading partner had manipulated its exchange rate.”¹⁴⁴

The Administration should take far more aggressive action on this issue. In particular, the Administration should make currency manipulation of the type practiced by China actionable under U.S. trade remedy laws, and should pursue legal action in the WTO to protect U.S. rights.

E. China as an NME

As demonstrated throughout this submission, China has not fully complied with its WTO obligations. Under these circumstances, the United States must effectively enforce its trade remedy laws. While this is not strictly a WTO “compliance” issue, trade law enforcement is essential for the United States to protect its rights and receive the benefits due under the WTO agreements.

Under the terms of its WTO accession, China agreed that other Members could treat it as a non-market economy (“NME”) for 15 years.¹⁴⁵ Nevertheless, China has urged the United States during recent meetings of the U.S.-China Strategic and Economic Dialogue to treat China as a “market economy” for purposes of U.S. AD laws.¹⁴⁶ This would be improper and contrary to U.S. law. U.S. law provides that in determining whether a country is an NME, the DOC must take six factors into account: (1) whether the country’s currency is convertible; (2) whether wage rates are determined by free bargaining between labor and management; (3) whether foreign investment is permitted in the foreign country; (4) whether the government owns or controls the means of production; (5) whether the government controls the allocation of resources and the price and output decisions of enterprises; and (6) such

¹⁴⁴ Statement by Treasury Secretary Timothy Geithner on Release of Semi-Annual Report to Congress on International Economic and Exchange Rate Policies (Apr. 15, 2009), *available at* <http://www.treas.gov> (last visited Aug. 26, 2009).

¹⁴⁵ *See* Protocol on the Accession of the People’s Republic of China at Section 15, part of *Accession of the People’s Republic of China*, WTO Doc. No. WT/L/432 (Nov. 23, 2001).

¹⁴⁶ U.S. Department of Treasury, *The First U.S.-China Strategic and Economic Dialogue Economic Track Joint Fact Sheet* (July 28, 2009), *available at* <http://www.treas.gov> (last visited Aug. 30, 2009).

other factors as the DOC considers appropriate.¹⁴⁷ In August 2006, the DOC conducted a detailed analysis of this issue and found that all six of these factors showed that China should continue to be treated as an NME.¹⁴⁸ Nothing has changed since that time that would warrant a different conclusion.

Another issue presented by China's NME status concerns the application of U.S. CVD law. Normally, in determining the benefit bestowed on the recipient of a non-recurring subsidy, the DOC will allocate the subsidy over the average useful life of the productive assets benefited by the subsidy.¹⁴⁹ In November 2007, the DOC decided for the first time to apply the CVD law to China.¹⁵⁰ Unfortunately, it determined that the "uniform date" from which it will identify and measure Chinese subsidies is December 11, 2001, the date on which China became a WTO member.¹⁵¹ In other words, non-recurring subsidies provided prior to this date are treated as though they were *not* subject to U.S. CVD laws.

AISI strongly disagrees with the DOC's decision on this issue. First, the decision fails to capture the full benefit of subsidies bestowed prior to China's WTO accession that have an average useful life that extends beyond December 11, 2001. Second, many of the subsidies provided prior to December 11, 2001 are extremely large and continue to provide countervailable benefits to this day. Finally, a condition of China's WTO accession was that it would become subject to subsidies disciplines, and Congressional approval of China's WTO accession was conditioned upon China's commitments in this regard. To decline to countervail subsidies bestowed prior to China's WTO accession is thus inconsistent with both China's WTO commitments and Congressional intent.

¹⁴⁷ See 19 U.S.C. § 1677(18)(B) (2000).

¹⁴⁸ Memorandum from Shauna Lee-Alaia, Lawrence Norton, and Anthony Hill to David M. Spooner, Assistant Secretary for Import Administration, Regarding Antidumping Duty Investigation of Certain Lined Paper Products from the People's Republic of China ("China") – China's Status as a Non-Market Economy ("NME") (Aug. 30, 2006) ("*August 30 Memorandum*") (Public Document).

¹⁴⁹ See 19 C.F.R. § 351.524.

¹⁵⁰ *Circular Welded Carbon-Quality Steel Pipe from the People's Republic of China*, Preliminary Affirmative Countervailing Duty Determination, 72 Fed. Reg. 63,875, 63,880 (Dep't of Commerce Nov. 13, 2007).

¹⁵¹ *Id.*

F. Enforcement of China-Specific Safeguard Provision

As part of its WTO accession, China agreed that for 12 years other members could impose product-specific safeguards against Chinese imports.¹⁵² This provision (implemented into U.S. law under Section 421 of the Trade Act of 1974, as amended)¹⁵³ is critical to ensuring that U.S. industries and workers do not suffer market disruption as a result of surges in Chinese imports. The provision was also critical in gaining support in the United States for China's WTO accession, and remains especially important given China's poor record of compliance with its WTO obligations.

Between 2002 and 2005, U.S. industries and workers brought six cases seeking relief under Section 421.¹⁵⁴ The ITC reached affirmative determinations under Section 421 in four of these cases.¹⁵⁵ However, in each of these cases, the previous Administration exercised its discretion to deny relief. As a result, until President Obama's recent decision to enforce Section 421, the statute had been effectively rendered a dead letter.

After the arrival of the new Administration this year, domestic producers of certain passenger vehicle and light truck tires filed a new petition seeking Section 421 relief with respect to imports from China – the first such petition since August 2005.¹⁵⁶ In July 2009, the ITC reached an affirmative determination in the case.¹⁵⁷ As part of its determination, the ITC recommended that the Administration impose a duty on imports of certain passenger vehicle and light truck tires from China for three years at rates up to 55 percent ad valorem.¹⁵⁸ The President's recent action to

¹⁵² See China's Protocol on Accession at ¶ 16.

¹⁵³ 19 U.S.C. § 2451 (2007).

¹⁵⁴ See USITC, Completed Trade Remedy Investigations, *available at* <http://www.usitc.gov> (last visited Aug. 26, 2009).

¹⁵⁵ See *Pedestal Actuators from China*, Inv. No. TA-421-1 (Determination), USITC Pub. 3557 (Nov. 2002); *Certain Steel Wire Garment Hangers from China*, Inv. No. TA-421-2 (Determination), USITC Pub. 3575 (Feb. 2003); *Certain Ductile Iron Waterworks Fittings from China*, Inv. No. TA-421-4 (Determination), USITC Pub. 3657 (Dec. 2003); *Circular Welded Non-alloy Steel Pipe from China*, Inv. No. TA-421-6 (Determination), USITC Pub. 3807 (Oct. 2005).

¹⁵⁶ See *Certain Passenger Vehicle and Light Truck Tires from China*, Inv. No. TA-421-7 (Determination), USITC Pub. 4085 (July 2009).

¹⁵⁷ *D.*

¹⁵⁸ *Id.* at 1.

provide relief in this case sends a strong signal that this mechanism of relief is now available to affected U.S. industries and workers.

AISI commends the Administration for providing relief in the Section 421 case on tires. This action sends an important signal that Section 421 is a viable remedy for U.S. companies and workers facing market disruption due to Chinese imports.. This action also has broader benefits to U.S. industry generally, as strong enforcement of U.S. trade laws is essential to obtaining the full benefits of China's WTO membership.

G. International Tax Rules – Border Adjustability

USTR has previously recognized that China manipulates its VAT system to help Chinese steel producers and other manufacturers.¹⁵⁹ At a larger level, there is an even more fundamental issue relating to VAT and border adjustability – an issue that significantly affects trade with China and other major trading partners. In particular, there is a fundamental disparity caused by international rules that unfairly reward countries like China (which rely on VAT systems) and penalize the United States (which relies principally on an income tax system). While this is not technically a compliance matter, it plays a significant role in our trade imbalance with China and other major trading partners.

Existing international rules allow countries relying on VAT systems to rebate indirect taxes on exports and apply them on imports while the United States is denied similar treatment for its “direct” (*i.e.*, income) tax system. As a result, U.S. exports to China and other major markets are essentially double-taxed, while Chinese and other foreign producers can sell here largely tax-free. By one estimate, this distortion of free trade represents a net disadvantage for U.S. exporters of more than \$100 billion per year.¹⁶⁰ There is no legitimate economic justification for such a practice.¹⁶¹

In 2002, when Congress approved trade promotion authority in the context of the Doha Round of WTO negotiations, it specifically provided that “[t]he principal

¹⁵⁹ See USTR 2008 Report at 40 (“Often, Chinese producers are able to avoid payment of the VAT on their products, either as a result of poor collection procedures, special deals, or even fraud, while the full VAT still must be paid on competing imports.”)

¹⁶⁰ Ernest Christian and Gary Hufbauer, “End this damaging tax and trade charade,” *Financial Times* (“Tax and Trade Charade”) at 11 (March 9, 2004).

¹⁶¹ Id.

negotiating objective of the United States regarding border taxes is to obtain a revision of the WTO rules with respect to the treatment of border adjustments for internal taxes to redress the disadvantage to countries relying primarily on direct taxes for revenue rather than indirect taxes.”¹⁶² Despite this clear instruction, very little has been done. In the Doha rules negotiations, while other countries have submitted literally dozens of papers attacking almost every aspect of U.S. trade remedy laws, the United States has not even submitted a single paper devoted to the issue of border adjustments. USTR should pursue this issue and do so aggressively.

H. Product Safety Issues

In recent years, safety concerns with Chinese imports have received a great deal of publicity in the United States.¹⁶³ There can be little doubt that these concerns extend to steel products. As Representatives Pete Visclosky (D-Ind.) and Tim Murphy (R-Pa.) stated in February 2009, “China has a proven track record of making dangerous, substandard products, including steel.”¹⁶⁴ Indeed, in July 2009, a series of significant welding flaws were discovered in certain Chinese steel products that were to be used in construction work on the San Francisco Bay Bridge.¹⁶⁵ The flaws were serious enough that the state of California sent top state officials to meet with the executives of the steel fabrication plant in an attempt to resolve the problem.¹⁶⁶

The issue of product safety implicates WTO concerns. Pursuant to China’s WTO accession, Chinese imports are subject to the WTO Sanitary and Phytosanitary Agreement, as well as the Agreement on Technical Barriers to Trade. Those agreements give the U.S. government broad authority to restrict imports that endanger the health and safety of Americans. The Administration should work with

¹⁶² Trade Act of 2002, P.L. 107-210, 116 Stat. 933, 1001 (Aug. 6, 2002) at § 2102(b)(15).

¹⁶³ See, e.g., “Chinese steel imports a safety risk: U.S. lawmakers,” *Reuters* (Apr. 30, 2008); “China product safety concerns have high stakes, far-reaching effects,” *SFGate.com* (Aug. 19, 2007); “China Lead Paint Crisis Spreads to Commercial Sector,” *ABCNEWS.com* (Aug. 23, 2007).

¹⁶⁴ U.S. Reps. Pete Visclosky and Tim Murphy, “Buy American to create jobs, revitalize economy” (Feb. 11, 2009), available at <http://www.nwi.com> (last visited Aug. 19, 2009).

¹⁶⁵ American Metal Market, “Chinese fabricator’s welding woes delay steel shipments for Bay Bridge” (July 29, 2009), available at <http://www.amm.com> (last visited Aug. 19, 2009).

¹⁶⁶ *Id.*

Congress to ensure that the U.S. government fully exercises its rights under the relevant WTO agreements to keep unsafe products out of this market.

I. Intellectual Property Rights

USTR has properly recognized that when China accepted the WTO Trade Related Aspects of Intellectual Property Rights (“TRIPS”) Agreement, it “took on obligations to adhere to generally accepted international norms to protect and enforce the intellectual property rights (“IPR”) held by U.S. and other foreign companies and individuals in China.”¹⁶⁷ Despite this agreement, however, USTR reports that “effective IPR enforcement has not been achieved, and IPR infringement remains a serious problem throughout China.”¹⁶⁸ This fact certainly concerns AISI’s members. Indeed, in its 2005 report, the USCC stated that China’s intellectual property violations “go well beyond the software and entertainment industries, *with many U.S. industrial firms now being heavily affected.*”¹⁶⁹

IPR represents another area in which dialogue between the United States and China has not been sufficient to bring China into compliance with its WTO obligations. The Administration recognized this fact in August 2007 when it requested a WTO dispute settlement panel to address IPR issues.¹⁷⁰ Significantly, U.S. concerns are not limited to a specific category of products; instead, they rest on the fact that “China has not provided for criminal procedures and penalties to be applied in cases of willful trademark counterfeiting or copyright piracy on a commercial scale that fail to meet certain thresholds.”¹⁷¹

In June 2009, the WTO adopted a panel report ruling that Chinese law does not adequately provide for the protection and enforcement of IPR on a wide range of products.¹⁷² Although the WTO’s findings represent a positive step forward, the

¹⁶⁷ USTR 2008 Report at 72.

¹⁶⁸ *Id.* at 77.

¹⁶⁹ USCC, “2005 Report to Congress” (Nov. 2005) at 41 (emphasis added).

¹⁷⁰ USTR, “United States Requests WTO Panel in Case Challenging Deficiencies in China’s Intellectual Property Rights Laws” (Aug. 13, 2007).

¹⁷¹ *China – Measures Affecting the Protection and Enforcement of Intellectual Property Rights – Request for the Establishment of a Panel by the United States*, WT/DS362/7 (Aug. 21, 2007).

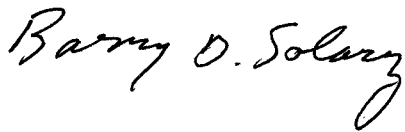
¹⁷² USTR, “World Trade Organization Adopts Panel Report in China – Intellectual Property Rights Dispute” (June 22, 2009).

Administration must ensure that China properly implements the recommendations and rulings of the WTO panel. Indeed, upon the announcement of the WTO's adoption of the panel report, U.S. Trade Representative Ron Kirk recognized that “[a] great deal of work remains for China to improve its IPR protection and enforcement regime.”¹⁷³ AISI urges the Administration to follow up with China to ensure that it does, in fact, implement the rulings and recommendations of the panel report.

III. Conclusion

This is AISI's sixth submission detailing China's non-compliance with its obligations under the WTO. When AISI made its first submission to the USTR in 2004, China produced 280 million MT of crude steel and held 26.2 percent of global market share.¹⁷⁴ Today, China is on pace to produce over 500 million MT of crude steel and has captured 48.5 percent of global market share.¹⁷⁵ These facts show that the United States' approach has not been effective in bringing China into compliance. Rather, China is continuing to use trade-distorting measures to build a massive steel industry that is injuring the U.S. steel industry, the U.S. economy, and the environment. The U.S. government must alter its approach so as to send a clear signal to China that it must end its trade-distorting policies and practices and comply with all of its WTO obligations.

Sincerely,



Barry D. Solarz

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¹⁷³ USTR, “World Trade Organization Adopts Panel Report in China – Intellectual Property Rights Dispute” (June 22, 2009).

¹⁷⁴ World Steel Association, “Steel Statistical Yearbook 2008” (2009), *available at* <http://worldsteel.org> (last visited Aug. 13, 2009) at 5. $280,486 / 1,069,082 = 0.262 = 26.2\%$.

¹⁷⁵ *See supra* note 20 and accompanying text.