

An hourglass-shaped graphic with a globe inside. The top bulb is dark blue, and the bottom bulb is light blue. The globe is a darker shade of blue. The hourglass is centered on the page.

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*United States' Trade Remedy Laws and Non-market Economies: A Legal Overview*

Todd B. Tatelman, American Law Division

April 23, 2007

**Abstract.** Several pieces of legislation have been introduced in the 110th Congress to specifically address the application of countervailing duty laws to non-market economies. These include, but are not limited to, H.R. 708, H.R. 910, H.R. 1127, H.R. 1229, S. 364, and S. 974.

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# United States' Trade Remedy Laws and Non-market Economies: A Legal Overview

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April 23, 2007

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## Summary

In the United States, there are two major forms of domestic trade remedy laws: antidumping law (AD), which combats the sale of goods at less than their fair market value, and countervailing duty law (CVD), which assess duties on imported goods to offset the amount of government or other public entity subsidization. Both of these remedies are available when the imported goods come from competitor countries that have free market policies. Since 1984, however, only AD law has been applied to those imported goods that come from non-market or other “transitional” economies. With the continued economic growth of some non-market and “transitional” economies, such as China and Vietnam, pressure has increased on the U.S. government to more aggressively utilize domestic trade remedy laws such as AD and CVD against unfair imports from these countries.

AD law has been amended several times since its initial inception in 1921. Each modern amendment has allowed for a new methodology for dealing with imports from non-market economies. With Congress’s continued statutory guidance, the Department of Commerce (DOC) has developed and implemented several different methodologies for applying AD law, even when the fair market value in the originating country is not readily ascertainable.

CVD law, however, has not been used against non-market economies since the DOC concluded in 1984 that it could not determine subsidization in such situations. This decision by the DOC was upheld as reasonable by the Court of Appeals for the Federal Circuit in *Georgetown Steel Corporation v. United States*. Since that time, with the noted exception of a 1991 petition against China, the DOC has refused to review CVD petitions against non-market economies. In November 2006, however, the DOC accepted a petition seeking a countervailing duty against imported “coated free-sheet paper” from China to offset alleged government subsidization. In April 2007, the DOC published a preliminary determination levying duties against the Chinese imports, as well as a memorandum distinguishing the Chinese economy from those economies that were at issue in the *Georgetown Steel* case.

While such an action appears to be consistent with U.S. law, a review of U.S. international obligations under the World Trade Organization’s (WTO’s) Agreement on Subsidies and Countervailing Measures, as well as China’s accession agreement to the WTO is also required. Both agreements appear to accept and sanction the use of surrogate country data in the application of domestic AD or CVD law. As a result, while a challenge to its actions at the WTO is always a possibility, the United States appears to have acted in a manner consistent with its obligations.

Several pieces of legislation have been introduced in the 110<sup>th</sup> Congress to specifically address the application of CVD laws to non-market economies. These include, but are not limited to, H.R. 708, H.R. 910, H.R. 1127, H.R. 1229, S. 364, and S. 974. This report will be updated as events warrant.

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## Introduction

In the United States, there are two major forms of domestic trade remedy laws: antidumping law (AD), which combats the sale of goods at less than their fair market value, and countervailing duty law (CVD), which assess duties on imported goods to offset the amount of government or other public entity subsidization. Both of these remedies are available when the imported goods come from competitor countries that have free market policies. Since 1984, however, only AD law has been applied to those imported goods that come from non-market or other “transitional” economies. With the continued economic growth of some non-market and “transitional” economies, such as China and Vietnam, pressure has increased on the U.S. government to more aggressively utilize domestic trade remedy laws such as AD and CVD against unfair imports from these countries.

## Antidumping Law (AD) and Non-market Economies

### Background

As generally applied, antidumping (AD) law considers dumping to have occurred when a foreign manufacturer charges a price that is “less than the fair market value” (LTFMV) for its product.<sup>1</sup> For dumping that is alleged from market-based economies, the Department of Commerce (DOC) employs a standard methodology for determining a product’s fair market value. First, the DOC determines whether a foreign manufacturer’s goods were sold in the United States for LTFMV by comparing the U.S. price of the product with the fair market value similar merchandise in the firm’s domestic market. If the product is not sold or offered for sale in the foreign firm’s domestic market, the DOC identifies the price at which the product is sold or offered for sale in countries other than the United States. Finally, if there are no sales in the home market or to third countries, the statute authorizes the DOC to utilize a “constructed value.”<sup>2</sup>

If the DOC finds that dumping has occurred, it establishes the “dumping margin” by calculating the average amount by which the product’s fair market value exceeds the price of the product in the United States.<sup>3</sup> The finding of dumping and the fixing of the “dumping margin” establish the first of the two prongs required to impose an AD duty. The final step in imposing an AD duty is an affirmative determination that the dumping has caused or threatens to cause a material injury to a U.S. industry.<sup>4</sup> The injury determination is made by the International Trade Commission (ITC), an independent agency.

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<sup>1</sup> See 19 U.S.C. § 1677 (2000).

<sup>2</sup> See 19 U.S.C. § 1677b(a)(2) (2000) (defining the use of constructed value); 19 U.S.C. § 1677b(e)(1) (2000) (providing the method of calculating a constructed value).

<sup>3</sup> 19 U.S.C. § 1673b(b)(1)(A) (2000).

<sup>4</sup> See 19 U.S.C. § 1677(7)(A) (2000) (stating that “[t]he term ‘material injury’ means harm which is not inconsequential, immaterial, or unimportant”). The statute requires that for “threatened injuries” the ITC support its findings by evidence that “the threat of material injury is real and that actual injury is imminent” and “not merely based on conjecture or supposition.” See 19 U.S.C. § 1677(7)(F)(ii) (2000).

## Application of AD Law to Non-market Economies: Various Approaches

As applied to non-market economies, the standard methodology described above causes problems because non-market economies do not allocate resources according to traditional market concepts of supply and demand, thereby making determinations of fair market value almost impossible. From the adoption of the Antidumping Act of 1921<sup>5</sup> until the passage of the Trade Act of 1974,<sup>6</sup> the application of AD law to non-market economies was devised and implemented exclusively through administrative agency action, as the statutes were silent. In the 1960s, the Treasury Department, which was, at the time, the agency with responsibility over domestic trade remedy laws, developed and began using what was known as the “surrogate country” approach for applying AD law to non-market economies. Under this approach, comparable prices and costs from similarly situated third countries were substituted for the non-market economy to determine fair market value.<sup>7</sup> This approach was adopted and codified by Congress in the Trade Act of 1974.<sup>8</sup> According to at least one legal scholar, “the surrogate methodology proved difficult to apply because there were occasions when there was no available surrogate. Therefore, it was necessary to devise an alternative methodology to use when an appropriate surrogate could not be located.”<sup>9</sup>

The Treasury Department responded to the concerns raised by the “surrogate country” approach by adopting a new methodology in 1975. This methodology, known as the “factors of production” approach, required that the amount of each factor input be taken from a market economy country considered to be at a comparable stage of economic development.<sup>10</sup> Congress expressly adopted this approach in the Trade Agreements Act of 1979, as an alternative to be used in non-market economy cases where there was no available surrogate country.<sup>11</sup>

In 1988, Congress again acted to adopt new AD provisions for dealing with non-market economies. In the Omnibus Trade and Competitiveness Act of 1988 (OTCA),<sup>12</sup> Congress enacted numerous reforms to the antidumping laws, starting with a definition of a non-market economy, as well as a set of standards that the DOC was to take into consideration when determining whether a specific country is a non-market economy. According to the OTCA, a non-market economy is a country that “does not operate on market principles of cost or pricing structures, so that sales of merchandise in such country do not reflect the fair value of the merchandise.”<sup>13</sup> The

<sup>5</sup> Antidumping Act of 1921, ch. 14 § 205, 42 Stat. 9, 13 (1921).

<sup>6</sup> Trade Act of 1974, P.L. 93-618, § 321, 88 Stat. 1978, 2074 (1974).

<sup>7</sup> See Department of Commerce, *Bicycles From Czechoslovakia*, 25 FED. REG. 6,657 (1960).

<sup>8</sup> See Trade Act of 1974, *supra* footnote 6.

<sup>9</sup> Robert H. Lantz, *The Search for Consistency: Treatment of Nonmarket Economies in Transition under United States Antidumping and Countervailing Duty Laws*, 10 AM. U. J. INT'L L. & POL'Y 993, 1003 (1995).

<sup>10</sup> See Department of Commerce, *Electric Golf Cars From Poland*, 40 FED. REG. 25,497 (1975).

<sup>11</sup> Trade Agreements Act of 1979, P.L. 96-39, § 776, 93 Stat. 144, 186 (1979) (codified as amended at 19 U.S.C. § 1677e). The act also transferred administrative authority from Treasury to the Department of Commerce who issued regulations outlining the hierarchy of methodologies to be used in determining the fair market value in AD investigations involving non-market economies. According to the DOC, market value should be determined according to (1) the home market prices of such or similar merchandise in a surrogate country; (2) the export price of such or similar merchandise shipped from a surrogate; (3) when actual or accurate prices are not available, the constructed value of such or similar merchandise in a surrogate country; and (4) the value in a surrogate country of the factors of production used in the non-market economy for such or similar merchandise. See 19 C.F.R. § 353.8 (a)-(c) (1979).

<sup>12</sup> Omnibus Trade and Competitiveness Act of 1988, P.L. 100-418, 102 Stat. 1107 (1988).

<sup>13</sup> 19 U.S.C. § 1677(18)(A) (2000).

factors the DOC must take into consideration when making a determination regarding a country's status as a non-market economy include

- (i) the extent to which the currency of the foreign country is convertible into the currency of other countries; (ii) the extent to which wage rates in the foreign country are determined by free bargaining between labor and management; (iii) the extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country; (iv) the extent of government ownership or control of the means of production; (v) the extent of government control over the allocation of resources and over the price and output decisions of enterprises; and (vi) such other factors as the administering authority considers appropriate.<sup>14</sup>

In addition, the OTCA provides the DOC with significant administrative discretion for determining when a foreign country is a non-market economy. According to the statute, the determination of non-market economy status may be made with respect to any foreign country at any time, and remains effective until expressly revoked by the DOC.<sup>15</sup> Moreover, the DOC's determinations are not subject to judicial review in any antidumping investigation.<sup>16</sup>

With respect to AD methodologies, the OTCA amended the AD laws to require that the "factors of production" approach was the preferred method of applying the law to non-market economies.<sup>17</sup> Despite this express statutory change, however, the DOC appears to have retained a significant amount of discretion with respect to its application. The legislative history of the OTCA seems to support the DOC's broad claims of discretion, indicating that the DOC is to determine on a case-by-case basis whether the available information permits the use of the standard methodology or whether a different approach is warranted.<sup>18</sup> As further evidence of its discretion to determine which approach to use when determining fair market value, the DOC stated that it would apply the various methodologies in the following order of priority:

- (1) prices paid by the [non-market economy] manufacturer for items imported from a market economy; (2) prices in the primary surrogate country of domestically produced or imported materials; (3) prices in one or more secondary surrogate countries reported by the industry producing the subject merchandise in the secondary country or countries, or; (4) prices in one or more secondary surrogate countries from sources other than the industry producing the subject merchandise.<sup>19</sup>

<sup>14</sup> 19 U.S.C. § 1677(18)(B) (2000).

<sup>15</sup> 19 U.S.C. § 1677(18)(C) (2000).

<sup>16</sup> 19 U.S.C. § 1677(18)(D) (2000).

<sup>17</sup> See 19 U.S.C. § 1677b(c)(2000) (stating that when "(A) the subject merchandise is exported from a nonmarket economy country, and (B) the administering authority finds that available information does not permit the normal value of the subject merchandise to be determined ... the administering authority shall determine the normal value of the subject merchandise on the basis of the value of the factors of production utilized in producing the merchandise and to which shall be added an amount for general expenses and profit plus the cost of containers, coverings, and other expenses.").

<sup>18</sup> See S. Rep. No. 100-71, 100<sup>th</sup> Cong., 1<sup>st</sup> Sess., 108 (1987) (stating that the bill "does not prohibit the [DOC] from using its normal methodology for determining foreign market value in cases regarding nonmarket economy countries. If information submitted by a non-market economy country to the [DOC] permits foreign market value to be determined accurately using the normal methodology, then the Committee expects such methodology to be used by the [DOC]."); see also Conf. Report No. 100-576, 100<sup>th</sup> Cong., 2<sup>d</sup> Sess. 591 (1988).

<sup>19</sup> Department of Commerce, *Final Determination of Sales at Less Than Fair Value: Sparklers from the People's Republic of China*, 56 FED. REG. 20,588 (1991).

The adoption by Congress of a specific statute authorizing the DOC to apply AD law to non-market economies, as well as providing legislative guidance with respect to acceptable methodologies—namely, authorizing various surrogate country approaches—has made AD law the exclusive remedy for U.S. industries when confronting unfair trade practices from non-market economies. As discussed below, however, the recent application—after a 23-year abstention by the DOC—of countervailing duty law to China, a non-market economy, would appear to potentially provide adversely affected industries with another option for combating unfair trade practices from non-market economies.

## Countervailing Duty Law (CVD) and Non-market Economies

### Background

Countervailing duty laws (CVD) are designed and intended to provide relief to domestic industries that have been, or are threatened with, the adverse impact from imported goods sold in the U.S. market that have been subsidized by a foreign government or other public entity. Specifically, the relief provided takes the form of an additional import duty on the subsidized imports. The duty levied is to be equal to the estimated amount of the government or other public subsidization. Similar to AD law, for an industry to obtain relief, both the ITC and the DOC must make conclusive determinations. The DOC must find that the targeted imports have been subsidized, and ITC must find that the domestic industry has been materially injured or threatened with material injury due to the subsidized imports.

### Application of CVD Law to Non-market Economies

Unlike the AD laws, however, U.S. CVD laws have not been traditionally applied to non-market economies. This is largely as a result of a 1984 determination by the DOC that there is no adequate way to measure market distortions caused by subsidies in an economy that is not based on market principles. The first determination by the DOC regarding the application of CVD law to non-market economies involved carbon steel wire rods manufactured in Czechoslovakia and Poland, both of which were non-market economies.<sup>20</sup> At the time of the DOC's decision, the United States had two separate CVD statutes. The first, § 303 of the Tariff Act of 1930,<sup>21</sup> applied

[w]henver any country, dependency, colony, province, or other political subdivision of government, person, partnership, association, cartel, or corporation, shall pay or bestow, directly or indirectly, any bounty or grant upon the manufacture or production or export of any article or merchandise manufactured or produced in such country, dependency, colony, province, or other political subdivision of government.<sup>22</sup>

<sup>20</sup> As many commentators have noted, however, this was not the first petition to be filed at the DOC relating to a non-market economy. In 1983, there was a CVD petition involving textiles from China, which was withdrawn prior to a ruling by the DOC. See e.g., Sanghan Wang, *U.S. Trade Laws Concerning Nonmarket Economies Revisited for Fairness and Consistency*, 10 EMORY INT'L L. REV. 593, 598 n. 27 (citing Judith Hippler Bello & Alan F. Holmer, THE ANTIDUMPING AND COUNTERVAILING DUTY LAWS: KEY LEGAL AND POLICY ISSUES 146-48 (1987)).

<sup>21</sup> See Tariff Act of 1930, ch. 479, § 303 (1930). Section 303 of the Tariff Act of 1930 was repealed when the United States enacted the Uruguay Round Agreements Act of 1994 and subsequently joined the World Trade Organization. See Uruguay Round Agreements Act, P.L. 103-465, § 261(a), 108 Stat. 4809 (1994).

<sup>22</sup> See Tariff Act of 1930, ch. 479, § 303 (1930).

The second CVD statute, section 701(b) of the Tariff Act of 1930, was enacted as part of the Trade Agreements Act of 1979 and intended to bring the United States into compliance with the Agreement on the Interpretation and Application of Articles VI, XVI, and XXIII of the General Agreements on Tariffs and Trade (Subsidies Code) that had been negotiated in Geneva under the auspices of the General Agreements on Tariffs and Trade (GATT).<sup>23</sup> Section 701(b) applied CVD law to “a country under the Agreement” and required that the United States first make a determination that the subsidized imports either caused, or threatened to cause, material injury to an industry in the United States, or caused the establishment of an industry in the United States to be materially retarded.<sup>24</sup>

Because neither Poland nor Czechoslovakia were signatories to the 1979 Subsidies Code, the DOC conducted its investigations of the alleged subsidization of carbon wire steel rod pursuant to section 303 of the Tariff Act.<sup>25</sup> At the preliminary determination stage, the DOC found that the phrase “any country” meant that no government entity could be excluded on a *per se* basis from the CVD law.<sup>26</sup> At the final determination stage, however, the DOC indicated that it had failed to address a second jurisdictional element, namely, “whether government activities in a [non-market economy] confer a ‘bounty or grant’ within the meaning of section 303.”<sup>27</sup> In evaluating this element, the DOC determined that countervailable subsidies cannot, conceptually speaking, be found within a non-market economy and, therefore, cannot be included within the scope of the phrase “bounty or grant.”<sup>28</sup>

To justify its final determinations, the DOC relied on the rationale that a subsidy is an action taken by a government or other public entity that distorts or subverts the operation of the free market. Since all costs, prices, and profits in non-market economies are centrally controlled (i.e., by the state), the concept of subsidization is arguably meaningless as there are no market forces to subvert or distort. In other words, because a subsidy is essentially a market phenomena, it has no meaning or purpose in a non-market economy.<sup>29</sup> In addition, according to the DOC, while resources may in fact be allocated inefficiently relative to a similarly developed market economy, it is impossible to state with any degree of certainty whether the misallocation results from subsidization, or from central planning.<sup>30</sup> Furthermore, the DOC noted a practical problem with determining the amount of subsidization from a non-market economy. Specifically, the DOC stated that because all economic activity in a non-market economy is centrally controlled, there exists no way to practically “disaggregate government action in such a way as to identify the exceptional action that is a subsidy.”<sup>31</sup>

The DOC, in determining that its conclusion was consistent with its statutory authority, conducted a review of the applicable CVD statutes and their legislative histories. Based on this review, the DOC held that “Congress has never confronted directly the question of whether the

<sup>23</sup> See Trade Agreements Act of 1979, P.L. 96-39, §§ 103, 105(a), 93 Stat. 190, 193 (1979).

<sup>24</sup> *Id.*

<sup>25</sup> Department of Commerce, *Carbon Steel Wire Rod From Czechoslovakia; Final Negative Countervailing Duty Determination*, 49 FED. REG. 19,370, 19,371 (May 7, 1984).

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> See *id.*

<sup>30</sup> *Id.*

<sup>31</sup> *Id.* at 19,372.

countervailing duty law applies to [non-market economy] countries.”<sup>32</sup> The DOC pointed to amendments to U.S. trade remedies law made by Congress in both 1974 and 1979 to justify its determination. The DOC noted in particular that, while Congress addressed import violations by non-market economies by adopting section 406 of the Trade Act of 1974 and by making changes to the antidumping laws, it declined to make corresponding changes to CVD law.<sup>33</sup> Therefore, in light of Congress’s silence with respect to the application of CVDs to imports from non-market economies, the DOC concluded that, as the administering agency, it possessed broad discretionary authority with respect to the question of whether a countervailable subsidy could exist in a non-market economy situation.<sup>34</sup>

## Court of International Trade’s Decision

Reviewing the DOC’s final determinations, the Court of International Trade (CIT), in *Continental Steel Corp. v. United States*,<sup>35</sup> disagreed with the agency’s conclusion that subsidies cannot by definition exist within a non-market economy. As a result, the CIT reversed and remanded the case back to the DOC for further investigation.

The CIT took specific issue with two of the DOC’s holdings. First, the CIT noted that the DOC committed a “fundamental error” in its premise that a subsidy can only exist in a market economy.<sup>36</sup> Second, the CIT argued that the DOC’s determination was “at odds with the plain meaning and purpose of the law,” “contradicts judicial interpretations of the law,” and is “inconsistent with past administration of the law.”<sup>37</sup> Regarding its second point, the CIT noted that section 303 of the Tariff Act of 1930 “makes no distinctions based on the form of any country’s economy,” and “on its face shows a meticulous inclusiveness and an unwavering intention to cover all possible variations of the acts sought to be counterbalanced.”<sup>38</sup> According to the CIT, the DOC’s adoption of a *per se* rule that subsidies cannot exist in non-market economies served to effectively amend CVD law by administrative fiat and, therefore, was irrational, arbitrary, and contrary to law.<sup>39</sup>

Regarding the DOC’s determination that subsidies are purely a market phenomena and thus not applicable to non-market economies, the CIT argued that the problem is essentially one of measurement and not one of meaning.<sup>40</sup> The CIT pointed to the application of antidumping law to non-market economies and noted that the use of surrogate or other substitute values for free market values does not deter the DOC from determining dumping margins; therefore, the absence of free market values similarly should not serve to deter or prevent the DOC from being able to calculate subsidy margins.<sup>41</sup>

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<sup>32</sup> *Id.* at 19,373.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at 19,374 (citing *United States v. Zenith Radio Corp.*, 562 F.2d 1209, 1316 (Fed. Cir. 1977), *aff’d*, 437 U.S. 443 (1976)).

<sup>35</sup> *Continental Steel Corp. v. United States*, 614 F. Supp. 548 (Ct. Int’l Trade 1985).

<sup>36</sup> *Id.* at 550.

<sup>37</sup> *Id.*

<sup>38</sup> *Id.* at 551.

<sup>39</sup> *Id.* at 552.

<sup>40</sup> *Id.* at 554.

<sup>41</sup> *Id.* at 555.

## Federal Circuit's *Georgetown Steel* Decision

Subsequently, in *Georgetown Steel Corp. v. United States*,<sup>42</sup> the Court of Appeals for the Federal Circuit reversed the CIT and reinstated the DOC's conclusions. The court, focusing first on the DOC's holding that the terms "bounty and "grant" as contained in section 303 of the Tariff Act of 1930 were not intended to apply to non-market economies, held that the question could not be answered by relying on the statute's plain language.<sup>43</sup> The court noted that when the statute was initially enacted in 1897, there were no non-market economies; therefore, Congress had no reason to have addressed the issue.<sup>44</sup> According to the court, the fact that in the six subsequent amendments to the CVD statute Congress made no attempt to address the issue of the statute's application to non-market economies "strongly suggests that Congress did not intend to change the scope or meaning of the provision that it had first enacted in the last century."<sup>45</sup>

The court then discussed the two most recent amendments to the CVD laws and observed Congress's belief, as evidenced by both the acts themselves and their legislative histories, that

changes in the antidumping law were necessary to make that law more effective in dealing with exports from nonmarket economies, coupled with its silence about application of the countervailing duty law to such exports, strongly indicates that Congress did not believe that the latter law covered nonmarket economies.<sup>46</sup>

In other words, according to the court, Congress intended to deal with imports from non-market economies being sold at unreasonably low prices under antidumping law, not CVD law.<sup>47</sup>

In conclusion, the court, relying on accepted principles of administrative law, afforded the DOC substantial deference with respect to its decisions regarding the application of CVD law to non-market economies. Specifically, the court held that the DOC has broad discretion in determining the existence of a subsidy under U.S. CVD law,<sup>48</sup> and that the DOC's conclusion that subsidies cannot be found in non-market economies was reasonable, in accordance with the law, and not an abuse of discretion.<sup>49</sup>

## Post *Georgetown Steel* Decisions

As a result of the Federal Circuit's decision in *Georgetown Steel*, there were no other countervailing duty investigations of allegedly subsidized imports from non-market economies until 1991. That year, the DOC did have occasion to examine a petition alleging the subsidization of ceiling and oscillating fans imported from China.<sup>50</sup> Although China is considered a non-market

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<sup>42</sup> *Georgetown Steel Corp. v. United States*, 801 F.2d 1308 (Fed. Cir. 1986).

<sup>43</sup> *Id.* at 1314.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.* (citing S. Rep. No. 249, 96<sup>th</sup> Cong., 1<sup>st</sup> Sess. 43 (1979), reprinted in 1979 U.S.C.C.A.N. 381, 429 (1979)).

<sup>46</sup> *Id.* at 1317.

<sup>47</sup> *Id.* at 1318.

<sup>48</sup> *See id.* at 1318 (citing *United States v. Zenith Radio Corp.*, 562 F.2d 1209, 1219 (Fed. Cir. 1977). *aff'd* 437 U.S. 443 (1978)).

<sup>49</sup> *Id.* at 1318 (citing *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-45 (1984); *Melamine Chemicals, Inc. v. United States*, 732 F.2d 924, 928 (Fed. Cir. 1984)).

<sup>50</sup> Department of Commerce, *Final Negative Countervailing Duty Determinations: Oscillating and Ceiling Fans From* (continued...)

economy, the petition was based on the theory that this particular industry was sufficiently market-oriented that the DOC could reliably use the economic data provided by the industry itself consistent with the standards utilized for CVD investigations in market economies.<sup>51</sup>

According to the DOC, to determine whether an industry is sufficiently market-oriented, a three-part test is utilized. First, “there must be virtually no government involvement in setting prices or amounts to be produced.”<sup>52</sup> Second, the industry “should be characterized by private or collective ownership. There may be state-owned enterprises in the industry, but substantial state ownership would weigh heavily against finding a market-oriented industry.”<sup>53</sup> Finally, “[m]arket-determined prices must be paid for all significant inputs, whether material or non-material (e.g., labor and overhead), and for an all-but-insignificant proportion of all the inputs accounting for the total value of the merchandise under investigation.”<sup>54</sup> The DOC ultimately concluded that, while some of the inputs for the ceiling and oscillating fans were in fact obtained from market sources, there remained a significant portion of the inputs that were not and, therefore, the industry as a whole did not qualify as a market-oriented industry.<sup>55</sup> As a result of this determination, the DOC held that CVD law did not apply to the Chinese ceiling and oscillating fan industry.<sup>56</sup>

Some commentators and scholars have objected to this so-called market-oriented industry approach because the test, especially the third prong, almost guarantees that no such industries will be found.<sup>57</sup> In addition, some critics have contended that the DOC’s determination that “significantly all” factor input prices must be market-driven is ambiguous and may lead to arbitrary results. Such arbitrary results, according to critics, arguably play a role in creating uncertainty for non-market economy producers with respect to U.S. trade remedy laws.<sup>58</sup> Furthermore, it appears possible to argue that under this approach, a non-market economy can enact substantial market based reforms while remaining immunized from CVD investigations.<sup>59</sup>

Although the DOC’s determination in *Oscillating and Ceiling Fans From the People’s Republic of China* appears to have opened the door to the potential application of CVD law to non-market

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(...continued)

*the People’s Republic of China*, 57 FED. REG. 24,018 (June 5, 1992).

<sup>51</sup> *Id.* at 24,018.

<sup>52</sup> *Id.*

<sup>53</sup> *Id.*

<sup>54</sup> *Id.*

<sup>55</sup> *Id.* (stating that “[b]ased on our verification of the responses submitted in this proceeding, we determine that the fans industry in the PRC does not meet the third of these criteria”).

<sup>56</sup> *Id.* at 24,019 (concluding that “we have determined that the PRC fans industry is not [a market-oriented industry]. As a result, we determine that the CVD law cannot be applied to the PRC fan industry.”).

<sup>57</sup> Lawrence J. Bogard & Linda C. Menghetti, *The Treatment of Non-Market Economies Under U.S. Antidumping and Countervailing Duty Law: A Petitioner’s Perspective*, PLI Corp. Law and Practice Course Handbook, Series No. 789, 6-7 (1992); see also James K. Kearney & Jim Wang, *The Department of Commerce’s Market-Oriented Industry Methodology for Nonmarket Economies in Antidumping Investigations: The Responding Party’s Perspective*, PLI Corp. Law & Practice Handbook Series No. 789, 255, 266-67 (1992).

<sup>58</sup> See James K. Kearney & Jim Wang, *The Department of Commerce’s Market-Oriented Industry Methodology for Nonmarket Economies in Antidumping Investigations: The Responding Party’s Perspective*, PLI Corp. Law & Practice Handbook Series No. 789, 255, 266-67 (1992).

<sup>59</sup> See Lawrence J. Bogard & Linda C. Menghetti, *The Treatment of Non-Market Economies Under U.S. Antidumping and Countervailing Duty Law: A Petitioner’s Perspective*, PLI Corp. Law and Practice Course Handbook, Series No. 789, 9-11 (1992).

economies, the DOC did not accept another CVD petition against a non-market economy until 2006.

## Recent Application of CVD Law to “Coated Free-Sheet Paper” Imports from China

On November 27, 2006, the DOC announced that it had initiated a CVD investigation against China with respect to “coated free-sheet paper.”<sup>60</sup> On April 9, 2007, the DOC announced, via publication in the *Federal Register*, that it had made an affirmative preliminary determination of subsidy in the CVD investigation with respect to imports from China. The DOC calculated preliminary estimated net countervailable subsidy rates ranging from 10.9% to 20.35%.<sup>61</sup>

Between the initiation of the investigation and the DOC’s preliminary findings, the Government of the People’s Republic of China sought an injunction from the United States Court of International Trade to prevent the DOC from conducting the CVD investigation.<sup>62</sup> China argued that the court had proper jurisdiction to hear the claim for an injunction and that the DOC was prohibited by *Georgetown Steel* from conducting CVD investigations.<sup>63</sup> Therefore, according to the Government of China, Congress is required to pass a statute expressly authorizing the application of CVD law against non-market economies.<sup>64</sup> The United States responded by asserting that the court did not have appropriate jurisdiction to hear the claim until DOC issues its final determination in the CVD investigation; therefore, this case was not ripe for adjudication.<sup>65</sup> Further, the United States argued that there is no statutory or other legal prohibition on the application of CVD law on non-market economies; therefore, China’s request for an injunction should be denied.<sup>66</sup>

<sup>60</sup> See Department of Commerce, *Notice of Initiation of Countervailing Duty Investigations: Coated Free Sheet Paper From the People’s Republic of China, Indonesia and the Republic of Korea*, 71 FED. REG. 68,546 (November 27, 2006).

<sup>61</sup> See Import Administration, International Trade Administration, Department of Commerce, *Coated Free Sheet Paper From the People’s Republic of China: Amended Preliminary Affirmative Countervailing Duty Determination*, 72 FED. REG. 17,484 (April 9, 2007).

<sup>62</sup> See *Government of the People’s Republic of China v. United States*, \_\_\_ F. Supp. 2d \_\_\_, 2007 WL 951808, \*1 (Ct. Int’l Trade 2007).

<sup>63</sup> *Id.* at \*2 (arguing that “[28 U.S.C. §] 1581(i) is available to them because the other potential vehicle for judicial review of their claims-filing suit under 28 U.S.C. § 1581(c) FN5 after Commerce completes the investigation-is manifestly inadequate.”).

<sup>64</sup> *Id.* at \*3 (asserting that “Commerce does not have the discretion to apply countervailing duty law to [non-market economies] because the [Court of Appeals for the Federal Circuit] “definitively ruled” that the countervailing duty statute “may not be applied to imports from NME countries.”).

<sup>65</sup> *Id.* at \*4 (arguing that “it is not possible to separate the merits of the decision from those relating to jurisdiction ... because in order for this Court to determine whether this investigation is ultra vires, it would have to determine whether CVD law could be applied to an [non-market economies]...” ... Moreover, the Government adds, this Court lacks jurisdiction on ripeness grounds because [DOC] has not yet taken final agency action.”) (internal citations and quotation marks omitted).

<sup>66</sup> *Id.* at \*5 (asserting that “neither the countervailing duty statute nor [DOC’s] rules limit the agency’s power to initiate countervailing duty investigations of [non-market economies]. ... *Georgetown Steel* did not hold that the CVD law could never apply to [non-market economies] under any circumstances, but only that [DOC’s] decision not to apply it in that case was reasonable.”).

The Court of International Trade declined to issue the injunction. Focusing primarily on the jurisdictional issues, the court held that the Government of China and the other plaintiffs will have a “sufficient opportunity” to seek judicial review of their claims after the DOC completes its investigation and issues a final determination.<sup>67</sup> While the court did address the applicability of *Georgetown Steel*—concluding that “it is not clear that Commerce is prohibited from applying countervailing duty law to [non-market economies]. Nothing in the language of the countervailing duty statute excludes [non-market economies]”<sup>68</sup>—its holding with respect to *Georgetown Steel* and its meaning is arguably *dicta*, as it does not appear to have been necessary to the conclusion that the court lacked jurisdiction.

In publishing its preliminary findings, the DOC also issued a memorandum that directly confronts the *Georgetown Steel* precedent.<sup>69</sup> The memorandum provides a justification as to why China’s economy in 2005, the period for which the investigation is concerned with, and the so-called “Soviet-style economies” are distinguishable, such that it is now possible to apply CVD law to some non-market economies.<sup>70</sup>

It is important to note that the memorandum and preliminary CVD determination do not in any way change or alter China’s formal status as a non-market economy.<sup>71</sup> Rather, the memorandum and justification focus on whether the rationale used to prevent CVD law from applying to non-market economies in 1984 remains true for modern-day China. The memorandum concerns itself with five major areas of the Chinese economy: wages and prices, access to foreign currency, personal property rights and private entrepreneurship, foreign trading rights, and allocation of financial resources.<sup>72</sup> While the specific economic analysis and details are beyond the scope of this report, the memorandum concludes that, unlike the so-called “Soviet-style economies” at issue in *Georgetown Steel*, China’s present economy does not contain the same obstacles to determining the existence of subsidies. According to the memorandum,

private industry now dominates many sectors of the Chinese economy, and entrepreneurship is flourishing. Foreign trading rights have been given to over 200,000 firms. Many business entities in present-day China are generally free to direct most aspects of their operations, and to respond to (albeit limited) market forces. The role of central planners is vastly smaller.... Given these developments, we believe that it is possible to determine whether the PRC Government has bestowed a benefit upon a Chinese producer (i.e., the subsidy can be identified and measured) and whether any such benefit is specific. Because we are capable of applying the necessary criteria in the CVD law, the Department’s policy that gave rise to the

<sup>67</sup> See *id.* at \*6.

<sup>68</sup> See *id.* at \*7.

<sup>69</sup> See Memorandum titled Countervailing Duty Investigation of Coated Free Sheet Paper from the People’s Republic of China - Whether the Analytical Elements of the *Georgetown Steel* Opinion are Applicable to China’s Present-Day Economy, from Shauna Lee-Alaia & Lawrence Norton, Office of Policy, Import Administration to David M. Spooner, Assistant Secretary for Import Administration, March 29, 2007, available at, <http://ia.ita.doc.gov/download/prc-cfsp/CFS%20China.Georgetown%20applicability.pdf> (hereinafter *Georgetown Steel* Memo).

<sup>70</sup> See *id.*

<sup>71</sup> See *id.* at 2-4 (noting that the DOC’s recent review of China’s non-market economy status concluded that “while China has enacted significant and sustained economic reforms, the PRC Government has preserved a significant role for the state in the economy. Indeed, the limits the PRC Government has placed on the role of market forces are sufficient to preclude China’s designation as a market economy under the U.S. antidumping law.”).

<sup>72</sup> See generally, *id.*

*Georgetown Steel* litigation does not prevent us from concluding that the PRC Government has bestowed a countervailable subsidy upon a Chinese producer.<sup>73</sup>

## World Trade Organization Issues and Consistency

Neither federal agencies nor the federal courts are the exclusive forum for legal challenges to the application of U.S. countervailing duty and antidumping laws. Adversely affected countries may also have the right to challenge both preliminary and final antidumping and countervailing duty determinations before the Dispute Settlement Body of the World Trade Organization (WTO). The ability to initiate a dispute at the WTO, should U.S. CVD law be applied to a non-market economy, requires an analysis of the compatibility of such a requirement on U.S. WTO obligations under the WTO Agreement on Subsidies and Countervailing Measures (SCM Agreement). Based on not only the plain language of the SCM Agreement, but also the language of a recent Appellate Body (AB) decision, the use of what the WTO refers to as “substitute benchmarks” (which would appear to include the surrogate country methodology, as well as the factors of production, or market oriented industry approach) would in general appear to be consistent with U.S. international obligations. That being said, however, it may be the case that a specific application of a substitute benchmark may be found to be incompatible with U.S. WTO obligations on an “as applied” basis.

It would appear that the operative provision with respect to the use of substitute benchmarks is Article 14(d) of the SCM Agreement. Article 14(d) states, in relevant part, that

*... any method used by the investigating authority to calculate the benefit to the recipient conferred pursuant to paragraph 1 of Article 1 shall be provided for in the national legislation or implementing regulations of the Member concerned and its application to each particular case shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines: ... (d) the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).*<sup>74</sup>

The SCM Agreement’s use of the phrase “any method used” would appear to encompass not only existing U.S. practice regarding the use of surrogates in the “factors of production” methodology, but also the artificial pricing method discussed above. In addition, a recent Appellate Body (AB) ruling interpreting the scope of Article 14(d) concluded that “an investigating authority may use a benchmark other than private prices of the goods in question in the country of provision, when it has been established that those private prices are distorted, because of the predominant role of the government in the market as a provider of the same or similar goods.”<sup>75</sup> The AB went on to establish a limitation on the use of such benchmarks, requiring that their use must “relate or refer to, or be connected with, the prevailing market conditions in that country, and must reflect price,

<sup>73</sup> *Id.* at 10.

<sup>74</sup> WTO Agreement on Subsidies and Countervailing Measures, Art. 14(d), *available at*, [http://www.wto.org/english/docs\\_e/legal\\_e/24-scm.pdf](http://www.wto.org/english/docs_e/legal_e/24-scm.pdf) (emphasis added).

<sup>75</sup> Report of the Appellate Body, *United States—Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R ¶ 103 (2004).

quality, availability, marketability, transportation and other conditions of purchase or sale, as required by Article 14(d).<sup>76</sup> Nevertheless, the AB expressly refused to suggest or rule upon specific alternative methods that might be available to countries, noting that such a review would be appropriate only on a case-by-case basis.<sup>77</sup>

Further evidence suggesting the consistency of the use of either surrogate countries, factors of production, or other “substitute benchmarks” with respect to non-market economies may be derived from China’s Accession Agreement to the WTO.<sup>78</sup> Adopted in November of 2001, the Agreement governs China’s accession to the WTO and has become an integral part of the WTO Agreement. Because China is currently classified by the United States and other countries as a non-market economy,<sup>79</sup> the language with respect to the application of the SCM Agreement appears to be relevant to any discussion of the application of trade remedy laws to non-market economies. Article 15(b) of China’s Accession Agreement indicates that when applying the relevant provisions of the SCM Agreement,

if there are special difficulties in that application, the importing WTO Member may then use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks. In applying such methodologies, where practicable, the importing WTO Member should adjust such prevailing terms and conditions before considering the use of terms and conditions prevailing outside China.<sup>80</sup>

This language appears to recognize the inherent difficulties in calculating a subsidy or dumping margin using values obtained from non-market economies. Moreover, the language seems to indicate that, provided that the use of benchmarks can be adjusted to meet the prevailing economic terms and conditions, their use is both acceptable by China and permissible under WTO obligations. It should be noted, however, that while it may be possible to argue that the use of benchmarks is not a violation of WTO obligations on their face, their application to a specific industry or imported product may still be subject to challenge on an “as applied” basis.

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<sup>76</sup> *Id.*

<sup>77</sup> *Id.* at ¶ 106 (stating that “[n]or are we required to determine the consistency with Article 14(d) of all the alternative methods mentioned by the participants and third participants; such assessment will depend on how any such method is applied in a particular case.”).

<sup>78</sup> See Protocol on the Accession of the People’s Republic of China, WT/L/432, available at, <http://www.wto.org> (November 23, 2001).

<sup>79</sup> Pursuant to China’s WTO accession protocol, the United States and other WTO members are allowed to treat China as a non-market economy for purposes of trade remedy laws through the year 2016. See *id.* at Art. 15(d). According to U.S. law, decisions to change China’s classification to a market economy must be made subject to the statutory requirements established by § 771(18)(b) of the Tariff Act of 1930 as added by the Trade Agreements Act of 1979. See Trade Agreements Act of 1979, P.L. 96-39 § 771, 93 Stat. 144 (1979) (codified as amended at 19 U.S.C. § 1677(18)(b) (2000)).

<sup>80</sup> See Protocol on the Accession of the People’s Republic of China, WT/L/432 Art. 15(b), available at, <http://www.wto.org> (November 23, 2001).

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