

WTO Industrial Subsidy Regulation: US-EU-Japan Joint Statement of January 2020 and Afterwards

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I. Introduction

On 14 January 2020 the United States, the European Union, and Japan (hereinafter referred to as “US-EU-Japan”) issued a trilateral joint statement,¹ proposing a set of new rules to strengthen WTO regulation on industrial subsidies. While a total of seven joint announcements have been made so far, this is the first time that three WTO Members have presented specific ideas on how to amend existing subsidy rules. Many of the proposed amendments seem to primarily target China’s trade policy and practices.

The talks between the three Members first took place in December 2017 when the MC-11 was held in Buenos Aires, Argentina. In the first trilateral joint statement, they expressed concerns over “severe excess capacity in key sectors exacerbated by government-financed and supported capacity expansion, unfair competitive conditions caused by large market-distorting

subsidies and state-owned enterprises, forced technology transfer, and local content requirements and preferences.”²

II. US-EU-Japan Joint Statement of 14 January 2020 to amend WTO subsidy rules

In the most recent joint statement of January 2020, US-EU-Japan proposed an amendment of the WTO Subsidies Agreement to (i) expand the scope of prohibited subsidies beyond the currently provided export subsidies and import substitution subsidies³ to include unlimited guarantees, subsidies to an insolvent or ailing enterprise in the absence of a credible restructuring plan, subsidies to enterprises unable to obtain long-term financing or investment from independent commercial sources operating in sectors or industries in overcapacity, and certain direct forgiveness of debt; (ii) provide for a reversal of the burden of proof in the case of harmful subsidies, including excessively large

1 Joint Statement of the Trilateral Meeting of the Trade Ministers of Japan, the United States and the European Union (2020.1.14), available at: <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2020/january/joint-statement-trilateral-meeting-tradeministers-japan-united-states-and-european-union>

2 Joint Statement by the United States, European Union and Japan at MC11”, USTR Press Release (2017.12.12.), available at: <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/december/joint-statement-united-states>

3 WTO Subsidies Agreement, Art. 3.1.

subsidies, subsidies to zombie enterprises,⁴ subsidies causing overcapacity,⁵ and certain input subsidies.⁶ Further, they proposed to (iii) make explicit that the subsidy can distort capacity and be linked to serious prejudice within the meaning of Article 6.3 of the WTO Subsidies Agreement; (iv) strengthen negative incentives or penalties applicable to subsidizing Members who fail to fulfill their notification obligations; (v) explicitly provide for detailed conditions and requirements to allow the investigating authorities to use out-of-country benchmarks in calculating the amount of benefit conferred (i.e. the amount of the subsidy which can be countervailed by the importing Member); and (vi) provide for a definition and criteria to determine whether a state-owned enterprise under investigation constitutes a “public body.”⁷

Among these elements, as will be discussed below in Section III of this Brief, it seems that the United States is paying particular attention to item (v), i.e. making explicit the possibility of using the out-of-country benchmark and on introducing necessary requirements to do so in measuring the benefit conferred and, ultimately, in calculating the amount of the countervailing duties (CVDs).

III. Draft General Council Decision of 20 Feb. 2020 additionally proposed by the United States

On 20 February 2020, approximately one month after the Joint Statement, the United

States submitted a communication to the WTO and proposed a draft General Council decision regarding “Market-oriented Conditions”⁸ under the WTO Agreement. In the proposal the United States stressed the need “to operate in a fairer and more open multilateral trading system” and requested the General Council to share its concerns with “non-market-oriented policies and practices that have resulted in damage to the world trading system and lead to severe overcapacity, create unfair competitive conditions for workers and businesses, hinder the development and use of innovative technologies, and undermine the proper functioning of international trade.” As the United States put it, “Members’ citizens and businesses should operate under market-oriented conditions,” and “market-oriented conditions are fundamental to a free, fair, and mutually advantageous world trading system, to ensure a level playing field.”

In this context, as an indicator for the existence of market-oriented conditions in a certain WTO Member the United States proposed the following elements:

Table 1. Illustrative Criteria to Determine the Existence of Market-Oriented Conditions

i	Decisions of enterprises on prices, costs, inputs, purchases, and sales are freely determined and made in response to market signals .
ii	Decisions of enterprises on investments are freely determined and made in response to market signals .
iii	Prices of capital, labor, technology, and other factors are market-determined .
iv	Capital allocation decisions of or affecting enterprises are freely determined and made in response to market signals .

⁴ “subsidies that prop up uncompetitive firms and prevent their exit from the market”. See *supra* note 1, para. 2.

⁵ “subsidies creating massive manufacturing capacity, without private commercial participation”. *Ibid*.

⁶ “subsidies that lower input prices domestically in comparison to prices of the same goods when destined for export”. *Ibid*.

⁷ WTO Subsidies Agreement, Art. 1.1.

⁸ Communication from the United States, “The Importance of Market-Oriented Conditions to the World Trading System,” Draft General Council Decision, WT/GC/W/796, 20 February 2020.

v	Enterprises are subject to internationally recognized accounting standards , including independent accounting.
vi	Enterprises are subject to market-oriented and effective corporation law, bankruptcy law, competition law, and private property law, and may enforce their rights through impartial legal processes , such as an independent judicial system.
vii	Enterprises are able to freely access relevant information on which to base their business decisions.
viii	There is no significant government interference in enterprise business decisions described above.

IV. Prospects and Implications for Korea

Based upon item (v) of the US-EU-Japan Joint Statement and the draft General Council decision by the United States, this Brief expects that there will be two layers of revision attempts of the WTO Subsidies Agreement.

Firstly, according to the draft General Council decision, the elements shown in Table 1 can work as criteria to determine that “market-oriented conditions exist”⁹ in a WTO Member. In a more practical sense, it means that the investigating authorities would be able to use these elements as evidence to determine that domestic price of the exporting country under investigation is distorted and cannot be used in calculating the amount of benefit conferred (i.e. the amount of the subsidy). If so, the investigating authorities would be able to resort to alternative benchmarks, including (i) proxies constructed on the basis of production costs; or (ii) “out-of-country” benchmarks such as world market

prices for similar products or market prices of like products in a third country.¹⁰

Although use of alternative benchmarks has been found to be WTO-consistent by the WTO adjudicating bodies in several cases, recently in *US - Countervailing Measures (China)* (Art 21.5 DSU)¹¹ the Appellate Body held that the United States acted inconsistently with Article 14(d) of the WTO Subsidies Agreement because the U.S. Department of Commerce failed to provide sufficient explanation to establish the Chinese government’s intervention in economy resulted in price distortion of China’s domestic inputs.¹² The United States Trade Representative (USTR) sharply criticized the Appellate Body ruling, arguing that it had “ignore[d] the findings of the World Bank, OECD working papers, economic surveys, and other objective evidence.”¹³

Presumably, it is against this background the United States has identified item (v) as its first priority for WTO amendment. China claimed the United States’ submission of a draft General Council decision is “quite an obvious ‘scene-setting’”¹⁴ or a diversion for its attempt to make a full-scale revision to existing WTO subsidy rules. However, given that the formal amendment to the WTO agreements requires (in practice) consensus among all WTO Members, from a practical standpoint this Brief finds the United States’ decision to prioritize item (v) strategically sound and (relatively) achievable.

Secondly, as a longer-term and more ambitious goal, a proposal could be submitted to include

⁹ Ibid., p. 1.

¹⁰ See, e.g., Appellate Body Report, US—Soft wood Lumber IV, WT/DS257/AB/R, 19 January 2004; Appellate Body Report, US—Carbon Steel (India), WT/DS436/AB/R, 8 December 2014.

¹¹ WT/DS437/AB/RW, 16 July 2019.

¹² Ibid., paras. 5.147-5.148.

¹³ USTR, “Statement on WTO Appellate Report on China Countervailing Duties” Press Release (2019.7.16), available at: <https://ustr.gov/about-us/policyoffices/press-office/press-releases/2019/july/statement-wto-appellate-report-china>.

¹⁴ “China: U.S. proposal merely ‘scene-setting’ for desired subsidy rules”, World Trade Online (March 3, 2020).

in the WTO Subsidies Agreement a similar definition of Non-Market Economies or NMEs as that of the United States' statute.¹⁵ Existing WTO law does not explicitly provide for a definition of NMEs.¹⁶ Thus in principle, it is left to the discretion of each Member whether to treat a certain country as an NME. Since 1981 the United States and the European Union have treated China as an NME in order to apply NME methodologies (the concept of which is roughly equivalent to alternative benchmarks under WTO subsidy rules) in calculating dumping margins against imports from China. In addition, starting from 2007 the U.S. Department of Commerce started to conduct anti-subsidy investigations against and imposed CVDs on Chinese imports in a number of cases. As opposed to GATT/WTO anti-dumping rules,¹⁷ however, the WTO Subsidies Agreement does not have any rules applicable to NMEs. For this reason the United States would have had no choice but to resort to Article 14 of the WTO Subsidies Agreement in order to use alternative benchmarks in lieu of distorted domestic prices of exporting countries under investigation – which turned out to be not quite successful for the United States, given recent WTO findings in *US - Countervailing Measures (China)* (Art 21.5 DSU). If an NME clause similar to that under WTO anti-dumping rules and/or Article 15 of China's WTO accession protocol were to be

incorporated into the WTO Subsidies Agreement, it would meaningfully increase the discretionary power of the investigating authorities in anti-subsidy cases.

In the case of Korea, since 1987 there has been no case of anti-subsidy investigation formally initiated to this day.¹⁸ Therefore, from the investigator's point of view it is expected that the suggested "market-oriented" criteria would not bring about any drastic changes to Korea's trade remedy law and practices. Also, if such elements were to be incorporated into the WTO Subsidies Agreement it would most likely provide that the investigating authorities "may" consider using alternative benchmarks or "may" designate other countries as an NME based on one or more than two of the above elements taken collectively, leaving broad discretion to each WTO Member. Thus with a high probability the Korea Trade Commission (KTC)¹⁹ would still be able to treat exporting countries the same way as before even after the amendment is successfully achieved.

From the viewpoint of an exporting country, however, the proposed amendment of item (v) could substantially affect future anti-subsidy investigations against Korea by major economies with frequent use of trade remedy measures. For instance, the same or similar reasoning as a "particular market situation" or a

15 19 U.S.C. Sec. 1677(18)(A): 'The term "nonmarket economy country" means any foreign country that the administering authority determines 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.' [Emphasis Added]

16 As an exception, GATT Ad Article VI:1, Note 2 indirectly mentions "a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State." Further, Article 2.7 of the WTO Anti-dumping Agreement makes reference to Ad Article VI:1, Note 2.

17 GATT Ad Article VI:1, Note 2, "in the case of imports from a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by

the State, [...] importing contracting parties may find it necessary to take into account the possibility that a strict comparison with domestic prices in such a country may not always be appropriate." [Emphasis added]

18 Korea Trade Commission, "Statistics on Trade Remedy," 16 March 2020, available at:

<https://www.ktc.go.kr/en/stats.do?menuId=94&tabIdx=1>

19 Korea Trade Commission was established in 1987, and was designated in January 1996 as the competent authority of anti-dumping and anti-subsidy investigations.

<https://www.ktc.go.kr/en/pageLink.do?link=/contents/en/introduce/history>

“PMS,” as has been numerous applied to imports from Korea²⁰ by the United States in anti-dumping investigation, could be applied in deciding upon the amount of CVDs. Among the proposed amendment elements in US-EU-Japan Joint Statement, it is thus noteworthy that at least item (v) might not work in Korea’s favour.

It is still premature to predict how the precise contents of the amendment will turn out, but sooner or later a time may come when Korea is asked to join the negotiations led by US-EU-Japan and needs to decide on its positioning as regards this issue. This Brief advises that the Korean government be readily prepared when that happens. In addition to continuous monitoring and a thorough legal and economic analysis on any further developments, this would require a comprehensive assessment of Korea’s current domestic industrial policy and practices. **KIEP**

20 PMS methodology has been applied to a number of Korean exports to the United States including OCTG, circular welded non-alloy steel pipe, welded line pipe, large diameter welded pipe, heavy walled rectangular welded carbon steel pipes and

tubes. See Chankwon Bae et al. 2018. A Study on Recent Changes in U.S. Trade Remedies: Cases Against Korean Exports, KIEP Policy Analysis 18-17, p. 98.