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Countervailing Calamity
How to Stop the Global Subsidies Race

by Scott Lincicome

Executive Summary

The world is awash in trade-distorting subsidies. Since the financial crisis of 2008, governments have adopted massive "stimulus" packages that have included taxpayer subsidies for industries, such as agriculture, alternative energy, and automobiles, which have distorted global markets, bred cronyism, and undermined free trade. These policies encouraged copycat subsidization, which spawned an increase in litigation at the World Trade Organization and led to the frequent imposition of protectionist duties via national countervailing duty (CVD) laws.

Trade reform is badly needed. Unfortunately, the U.S. government has little credibility on this issue: it is one of the world's largest subsidizers, funneling billions of dollars annually to chosen industries, causing economic uncertainty, and creating breeding grounds for corruption. Yet, ironically, with 59 currently active or pending CVD measures affecting over $11 billion of imports, the U.S. government is also one of the most frequent users of anti-subsidy disciplines.

However, the CVD law and its application are rife with problems because the Commerce Department has too much discretion administering the law, which exposes subsidy determinations to subjective and opaque decisionmaking. The CVD law is punitive instead of remedial, making victims of U.S. consumers and consuming industries, aggravating U.S. trading partners, and exposing U.S. businesses to retaliation against their exports and intellectual property.

By curtailing federal subsidies to favored industries and by reforming CVD procedures to ensure that they serve the rule of international trade law—rather than protectionist objectives—the U.S. government can reduce market distortions, restore some faith in free markets, and lead national and international subsidy reform initiatives.

Scott Lincicome is an international trade attorney with White & Case, LLP, and blogs on international trade issues at http://lincicome.blogspot.com. *The views expressed are his own.* *Special thanks to Jonathan Black for his invaluable research assistance.*

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Introduction

When the Department of Energy announced the bankruptcy of federal loan recipient Solyndra, the agency was quick to blame Chinese subsidies, rather than U.S. policy, for the failure. "Solar panel manufacturing is a growing international market," the DOE press release read, "with increasingly intense competition from Chinese manufacturers who are supported in many cases by interest-free government financing that is much more generous than what the U.S. provides." In one sense, the department had a point: Chinese and other subsidies distort global markets, strain public budgets, breed cronyism, and undermine public support for free trade and free markets. What the department downplayed, however, were the literally hundreds of state and federal subsidies—totaling billions of taxpayer dollars—that are available to U.S. producers and consumers of alternative or "green" energy products such as solar panels, wind towers, or biofuels. The Chinese government, on the other hand, was quick to note the hypocrisy.

A few months after the Solyndra news—but before the announced failures of a few other subsidized U.S. solar firms such as Abound Solar and First Solar—the U.S. government initiated antidumping and anti-subsidy (or "countervailing duty") investigations of Chinese solar panel producers. The legality of these cases is not in doubt. But as American solar manufacturers and their political friends shifted the blame for their failures to subsidized Chinese imports, they failed to mention that U.S. environmental goods exporters increasingly have been subject to similar investigations abroad, while U.S. green subsidies and U.S. countervailing duty procedures have come under increasing scrutiny—and indictment—at the World Trade Organization (WTO). Meanwhile, solar panel consumers around the world suffer the ill effects of the litigation and policy uncertainty surrounding trade in green goods.

Such problems are not isolated to Solyndra, or even to green subsidies. Since the financial crisis of 2008, the United States and many other nations established or expanded taxpayer subsidies for favored industries such as agriculture, alternative energy, and automobiles—subsidies which have since been found to harm just about everyone except the subsidy recipients and, of course, their political patrons. These policies have led to increased anti-subsidy litigation at the WTO and the imposition of more anti-subsidy measures via national countervailing duty cases.

In an ideal world of free-market statesmen, national and multilateral rules permitting remedial tariffs on subsidized imports would be unwelcome, if not unnecessary. Elected officials would resist the temptation to subsidize private commercial activity. They would welcome, rather than punish, subsidized imports from countries where governments chose to impoverish their citizens, distort their economies, and empty their public coffers for the benefit of foreigners' consumption. And, on the rare occasion when trade-distorting subsidies did persist, they would be eliminated through nonconfrontational negotiations.

Unfortunately, we do not live in an ideal world. Instead, most politicians in the United States and abroad—heavily influenced by well-organized producer lobbies—eagerly subsidize their preferred industries and view subsidized imports as an excuse to further funnel public resources to private ends. The result is a global subsidies race between governments to "invest" in favored industries to enhance the nation's "global competitiveness." The casualties from this free-for-all are numerous, and diplomatic attempts at a ceasefire have proven ineffective.

What should be done? Ignoring the problem—an attractive option to free-market advocates under many circumstances—would encourage more subsidies from abroad, more subsidies in response at home, and more protectionist actions that penalize U.S. consumers and consuming industries.

Anti-subsidy disciplines—such as those permitted under WTO agreements and codified under U.S. countervailing duty (CVD) law—could help. As the existence of the rule of law deters illegal activities, anti-subsidy rules and countervailing duty laws reduce the incentives to subsidize in the first place.

But the CVD law and its application are rife with problems. The Commerce Department has too much discretion administering the law, which exposes subsidy determinations to subjective and opaque decisionmaking, resulting too frequently in the imposition of duties significantly in excess of the value of subsidies allegedly being remedied. The CVD law is punitive instead of remedial, making victims of U.S. consumers and consuming industries, aggravating U.S. trading partners, and exposing U.S. businesses to retaliation against their exports and intellectual property.

The combination of metastasizing U.S. subsidy programs and growing foreign markets has exposed more U.S. exports to anti-subsidy litigation at the WTO and punitive countervailing duties at foreign borders. As growth in emerging economies continues and U.S. producers turn to those markets for sales revenues, more CVD cases are likely to be brought against U.S. exports. And once such measures are in place, they are difficult—if not impossible—to remove.

U.S. policymakers should recognize their strong interest in reforming U.S. subsidy programs and ensuring that other countries do the same. However, the only way that America can lead such a worthwhile endeavor is to overhaul its current approach to domestic and foreign subsidies. By curtailing targeted federal subsidies to favored industries and reforming its current CVD procedures, the U.S. government can begin to arrest and reverse the damage caused by the past few years of rampant government subsidization of industries worldwide. This paper provides the roadmap.

Subsidies and International Trade

Before examining the effects of global subsidies and the available policy responses, it is important to understand what is meant by a "subsidy." Broadly, a subsidy is anything provided by a government to assist an individual or business. The subsidies at issue here are those more narrowly defined in the WTO Agreement on Subsidies and Countervailing Measures (SCM Agreement) and codified into U.S. law as part of the Uruguay Round Agreements Act. This legal standard and its implications will be discussed more fully below.

Monitoring global subsidies can be difficult, but available evidence indicates a dramatic increase in their proliferation around the world since the financial crisis of 2008. The 2010 Organisation for Economic Co-operation and Development (OECD) report *Trade and Economic Effects of Responses to the Economic Crisis* found that governments had implemented "extensive" support measures between September 2008 and August 2009, and highlighted industrial subsidies to the automotive and environmental (or "green") sectors.[1] According to a March 2010 WTO report, in 2008 and 2009, governments "intervened heavily to stimulate growth and employment in specific industries or to avoid systemic collapse as in banking and finance."[2] Programs specifically mentioned in the report included consumption subsidies, state financing and credit assistance, direct and indirect support for "green" products and other favored industries, infrastructure projects, farm subsidies, and financial bailouts.[3] A few months later the WTO reinforced those findings by highlighting ample state support and trade-distorting production subsidies for the automotive, iron and steel, and textile and clothing industries.[4] The most recent (May 2012) version of the WTO report also found sustained—and in some cases increasing—levels of government subsidization, highlighting state support in various agricultural, industrial, and services sectors, as well as a rising number of complaints from WTO Members about subsidy programs that predate the financial crisis.[5] The report noted that these policies continued despite repeated commitments from governments to avoid protectionism and trade-distorting subsidies.

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fare. This is particularly true with regard to subsidies that encourage exports or that support specific sectors, which is why these categories are targeted by anti-subsidy rules. Subsidies also retard innovation by encouraging resource diversion from productive to political ends, such as lobbying for rules that limit competition. With respect to the post-crisis explosion of subsidies, an OECD analysis found that sector-specific production subsidies "yield overwhelmingly negative effects on the [domestic] economy, through maintaining or creating inefficiencies, and . . . yield negative pullovers on partner countries, through lowering production costs in one country relative to the world market."[6]

Subsidies also encourage cronyism. Politicians dole out subsidies to special-interest groups, who in turn lobby for more subsidies. As a result, subsidy policies are often based on political connections and privilege, rather than on social or economic grounds. A recent Mercatus Center study found extensive empirical support for the existence of such cronyism in U.S. subsidy policy, particularly related to Troubled Asset Relief Program (TARP) funding and housing subsidies. It concluded that cronyism not only can result in bad policy, but it also can undermine social cohesion and public support for capitalism and the political process.[7]

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Subsidies also lead to protectionist policy responses from importing countries that are lobbied by competing domestic industries and their workers to shield them from unfairly subsidized foreign competition. The two most common forms of such protectionism are anti-subsidy measures—most often countervailing duties—targeting the subsidized imports at issue, or domestic subsidies to counter the domestic harms caused by those imports. Each is described more fully below.

A Necessary Response to Subsidies: Global Anti-Subsidy Rules

U.S. policymakers can respond to subsidies in four basic ways: offset foreign subsidies with subsidies of our own, do nothing, conduct bilateral and multilateral negotiations on subsidy reform, and/or develop and utilize legitimate anti-subsidy disciplines.

In addressing the problem of trade-distorting global subsidies, global anti-subsidy disciplines are a necessary complement to international negotiations on subsidy reform. Responding with subsidies of our own merely exacerbates the problems identified throughout this paper and encourages a global subsidies race as more business groups and labor unions lobby their governments to commit greater shares of taxpayer resources to their industries in an attempt to "out-subsidize" their foreign competitors. For example, supporters of the U.S. Export-Import Bank (Ex-Im Bank) routinely defend that organization by claiming that its subsidies are necessary to "level the playing field" for U.S. firms whose rivals receive generous export credit subsidies from their own governments. Almost 40 percent of the Ex-Im Bank's loans are for this purpose.[8] That not only drains already empty federal coffers, but it undermines support for free trade and free markets.

A more legitimate argument exists, however, for doing nothing. From a pure free-market perspective, the United States should theoretically welcome other nations' use of subsidies, particularly in the trade context, because those nations are essentially subsidizing Americans' consumption, which, as Adam Smith famously noted in *The Wealth of Nations*, "is the sole end and purpose of all production." If another country wants to sell American citizens goods and services at artificially low prices, the U.S. government ought not get in the way.[9]

There are, however, sound economic and practical reasons for supporting the establishment and use of global subsidy disciplines to complement international negotiations on subsidy reform. As explained above, subsidies—particularly those targeting exports or specific sectors—distort markets and investment decisions. They lead to a misallocation of capital as resources are drawn to the production of goods and services that, but for the subsidy, would not otherwise be produced. In an increasingly integrated global economy of complex production and supply chains, national subsidies can have international implications. Moreover, targeted domestic subsidies act as a protectionist non-tariff barrier by artificially lowering prices in the domestic market of the subsidizing government. Thus, efforts to discourage subsidies can promote global welfare.

International agreements to eliminate or reform existing subsidy programs (and to avoid new ones) are worthwhile and can create ongoing diplomatic pressure for less distortive subsidy policies. However, as noted above, post-crisis attempts within the G20 and elsewhere to elicit government commitments to limit trade-distorting subsidies have proven only minimally effective, mainly as a check against serious backsliding rather than a strict prohibition or springboard for real reform. Thus, it is clear that a more direct policy approach is needed to complement negotiations.

Anti-subsidy disciplines can provide this lever because they more directly discourage the use of subsidies by offsetting recipients' potential export benefits and publicly shaming subsidizing governments. Such disciplines also can offset the political attractiveness of government subsidies by stigmatizing them as "illegal" and by establishing clear procedures, based on the rule of international trade law, for ensuring that the benefits of those subsidies will be neutralized. Many subsidy programs have been terminated on account of trade litigation, or the threat thereof, under global anti-subsidy rules that have been agreed upon voluntarily by all 157 WTO Member governments.

Moreover, anti-subsidy rules can discourage a protectionism arms race by providing legal, rather than only diplomatic, assurances that other governments' injurious subsidies will be neutralized. Politicians and rent-seeking interest groups often claim that subsidies are essential to offset the unfair advantages bestowed on subsidized foreign competition. This illogic is pervasive among protectionists in Congress, such as Sen. Sherrod Brown (D-OH), who routinely call for new U.S. protectionism in response to China's "improperly subsidizing manufacturing industries,"[10] but such thinking can infect even the most fiscally conservative members. For example, tea party icon Sen. Marco Rubio (R-FL), who represents sugar-producing Florida, recently justified his vote to protect the U.S. sugar program on the grounds that it is necessary to counteract foreign subsidies.[11] That sort of logic is what propels the spiral of tit-for-tat subsidization. Anti-subsidy rules can short-circuit the escalation by establishing that other governments' interventions will be neutralized without need of responding with commensurate subsidization at home.

Finally, it is important to distinguish anti-subsidy rules from antidumping disciplines. The dubious purpose of the latter is to assist certain U.S. producers that are struggling to compete with foreign suppliers in the U.S. market, while the purpose of the former is to identify, neutralize, and discourage anti-market *government* behavior. Whereas the intended result of an antidumping duty is to stop foreign suppliers from pricing so competitively in the United States, the intended result of a countervailing duty is the cessation of trade-distorting government subsidies.

That American policymakers across the political spectrum—in the face of massive federal budget deficits and amid ample evidence of the distortions they cause—openly support subsidies and cite foreign subsidy practices to excuse their own misbehavior is strong evidence that America's dangerous subsidy infatuation will continue without durable safeguards in place. Global anti-subsidy rules can provide that check, but steps must be taken to ensure that they are applied in a rational and equitable manner. The sections that follow demonstrate that United States is currently not taking those steps.

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The Origin of WTO Anti-Subsidy Rules and the U.S. Countervailing Duty Law

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the proliferation of trade-distorting subsidies and providing reasonable dispute-settlement mechanisms for adjudicating subsidy-related disputes. In order to ensure agreement among the anti-subsidy rules' original drafters and adherence by current and future WTO Members (essential elements of a voluntary multilateral trading system), WTO subsidy disciplines reflect a delicate compromise, discouraging only the most distortive government subsidies while allowing members to utilize broad-based subsidies at their discretion and limiting the protectionist administration of CVD laws by overzealous WTO Members.

Anti-subsidy measures typically take the form of import duties on the subsidized products at issue. The measures are intended to be remedial rather than punitive; that is, they are supposed to offset the value of the benefit of the subsidy to the foreign producers, so that it no longer confers a competitive advantage. Anti-subsidy measures are not intended to punish offending governments or their countries' exporters. Anti-subsidy actions may be adjudicated at both the national (through CVD investigations) and multilateral (through WTO dispute settlement) levels. The majority of anti-subsidy actions take the form of CVD investigations.

National CVD laws, including U.S. law, closely track WTO disciplines as set forth in the WTO Agreement on Subsidies and Countervailing Measures ("SCM Agreement"). In the United States, these rules are administered by the Department of Commerce (DOC), which is responsible for determinations of subsidization, and the U.S. International Trade Commission (ITC), which is responsible for determinations of injury. For countervailing duties to be imposed, affirmative findings of both foreign government subsidization and injury to a domestic industry must be made. The basic anti-subsidy disciplines are as follows:[12]

- A *subsidy* is defined as a"financial contribution" by a "government" or "public body" that confers a "benefit" on the recipient. This is the only globally accepted definition of a subsidy.
- A *financial contribution* is defined under the SCM Agreement and U.S. law[13] as existing in certain enumerated circumstances. These circumstances include a direct transfer of funds, (e.g., grants, loans, and equity infusion) or potential direct transfers of funds or liabilities (e.g. loan guarantees); government revenue that is otherwise due is forgone or not collected (e.g. tax credits or deductions); the provision of goods or services other than general infrastructure, or the purchase of such goods; and the "entrustment or direction" of a private entity to make any of the financial contributions listed above.
- A financial contribution must be provided by a *government* or a "*public body*," which has recently been defined by the WTO Appellate Body as "an entity that possesses, exercises or is vested with governmental authority."[14] Financial contributions by public bodies are automatically treated as if they come from the government itself; thus, no further analysis is required by an administering authority to determine whether a public body's transactions constitute a "financial contribution." A government or public body also may "entrust or direct" a non-governmental entity to provide a financial contribution, but this requires an additional and separate analysis based on the specific facts of the case.
- The determination of whether a "benefit" exists is based on the effect on the recipient, not the cost to the government. A benefit will exist where the recipient is "better off" than it otherwise would have been without the financial contribution, as determined by a comparison with a domestic, market-based benchmark.[15] The calculation of benefit using a market-based benchmark depends on the type of subsidy at issue. For certain subsidies, such as grants or tax breaks, this calculation is simple: the benefit is the amount of the grant or the amount of tax that would have been paid in the

absence of the exemption. In other circumstances, however, the benefit calculation can be far more complex, and the SCM Agreement provides additional guidelines to determine the existence of a "benefit" for the purposes of a countervailing duty investigation. For example:

  - With respect to government-provided loans or loan guarantees, a benefit exists where there is a difference between the amount that the firm receiving the loan/guarantee pays on its loan and the amount the firm would pay on a "comparable commercial loan" that the firm could actually obtain on the market without government involvement.
  - With respect to the purchase or provision of goods, a benefit exists where the government's purchase/provision of goods is made for "less than adequate remuneration," determined in relation to prevailing market conditions, which include price, quality, availability, marketability, transportation and other conditions of purchase or sale.[16]

- Not all subsidies may be subject to offsetting duties. Only subsidies that are *prohibited* (i.e., export subsidies and import substitution subsidies) or are *specific* to a domestic enterprise or industry (or group of enterprises/industries) may be countervailed or challenged at the WTO. These additional requirements reflect the preferences of WTO Members to permit broadly available subsidies—such as tax breaks for research and development or the construction of roads and ports—and discipline only those which more directly distort international trade and global competition.[17]
  - *Prohibited subsidies*. The SCM Agreement strictly prohibits two types of subsidies: export subsidies, defined as subsidies contingent, in law or in fact, upon export performance (e.g., a cash grant provided only on a domestic company's exports), and import substitution subsidies, defined as subsidies contingent upon the use of domestic goods over imported goods (e.g., a tax break for manufacturers who use domestic steel). Because prohibited subsidies have significant trade-distorting effects, they are subject to more rigorous disciplines at the WTO and under national countervailing duty laws. The SCM Agreement states that members "shall neither grant nor maintain" prohibited subsidies, and where a measure in question is found by a WTO panel to be a prohibited subsidy, the subsidizing member must "withdraw the subsidy without delay." In WTO dispute settlement, a finding that a prohibited subsidy also is specific or has injured complaining WTO Members' companies is unnecessary prior to the imposition of countermeasures. Under U.S. law, prohibited subsidies are deemed to be specific and thus countervailable.
  - *Specificity*. The SCM Agreement and U.S. law establish several principles to determine when a non-prohibited subsidy is "specific."[18] Most important, a subsidy may be specific in law (de jure) or fact (de facto). A subsidy is de jure specific where "the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises." However, if a granting authority, or the legislation under which the granting authority operates, establishes "objective criteria or conditions governing the eligibility for, and the amount of, a subsidy," then the subsidy will not be specific, "provided that the eligibility is automatic and that such criteria and conditions are strictly adhered to."[19] A subsidy is de facto specific where it is used by a limited number

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of certain enterprises, it is predominantly used by certain enterprises, it leads to the granting of disproportionately large amounts of subsidy to certain enterprises; or the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy indicates that one industry or enterprise has been favored above others.[20] A specific subsidy that is not prohibited is called an "actionable subsidy" in a WTO anti-subsidy dispute, while specific and prohibited subsidies are called "countervailable" subsidies under U.S. CVD law.

- *Injury*. Actionable (WTO dispute) or countervailable (U.S. law) subsidies may result in anti-subsidy countermeasures—typically duties on the subsidizing member's imports—where they are found to have injured the companies or industries of another WTO Member. In a WTO dispute, these "adverse effects" may take one of three forms: actual injury to the domestic industry of another member, "nullification or impairment of benefits accruing directly or indirectly to other Members under WTO rules," or "serious prejudice" to the interests of another member. In a CVD investigation, only "material injury"—or threat of such injury in the future—may suffice.

Although these legal standards may seem arcane, they are important because they reflect an agreement among all WTO Members as to the types of subsidies that they have voluntarily agreed to forgo (i.e., the most trade-distorting types) and the countervailing measures that they will accept on their exports when they are found to have imposed such subsidies in the face of agreed limitations. Because the multilateral trading system requires voluntary adherence by WTO Members, strict adherence to the letter of the law is critical to maintaining the system's legitimacy. Thus, it is essential that all WTO Members follow the aforementioned anti-subsidy rules in terms of both the types of subsidies permitted and the principles and procedures for imposing anti-subsidy measures. Unfortunately, many nations, including the United States, fail to adhere to these agreed disciplines and thereby imperil legitimate efforts to discourage subsidies and the overall health of the global trading system.

The United States—Big Subsidizer, Big Anti-Subsidizer

U.S. subsidy policy reflects a "do as I say, not as I do" approach to trade and economic issues. Despite the obvious economic, legal, and political problems associated with domestic subsidies, the United States remains one of the world's largest subsidizers. Yet the U.S. government also is one of the most frequent users of anti-subsidy disciplines, which have spiked in recent years.

Since the financial crisis of 2008, global anti-subsidy actions and U.S. involvement in these cases have increased dramatically. According to the WTO, CVD case initiations and U.S. participation—as either a targeted exporter/government or the initiator—almost doubled between 2004–2007 and 2008–2011. In each period, the United States was involved in more than half of all CVD investigations.

There also have been 16 subsidy-related disputes at the WTO since 2008. The United States has been a respondent in 4 and a complainant in 6 of those disputes.[21]

The increased anti-subsidy activity correlates with the onset of both the global economic downturn and government policies supporting strategic industries through stimulus and export promotion efforts. Given that the United States, and the global economy more broadly, will continue to face economic pressures, it is logical to assume that anti-subsidy actions will continue at an elevated level for the foreseeable future. U.S. subsidy and anti-subsidy policies practically guarantee it.

The U.S. federal government continues to be one of the world's largest subsidizers. According to a new Cato Institute report, the United States will spend $98 billion on business subsidies—including direct and indirect subsidies to small businesses, large corporations, and industry organizations—for fiscal 2012.[22] Despite immense federal budget pressures, total business subsidies are actually up significantly from about $90 billion in 2009.[23] Moreover, the United States has spent approximately $2.5 *trillion* on "temporary" fiscal stimulus measures since 2008.[24] A thorough accounting of all such subsidies is beyond the scope of this paper, but several programs deserve emphasis because they target specific industries and consume a disproportionate share of the federal budget:

Agriculture. Perhaps no industry has attracted more taxpayer dollars (and global ire) than U.S. agribusiness. According to the Environmental Working Group's compilation of United States Department of Agriculture data, the U.S. government has provided approximately $277.3 billion in subsidies to U.S. farms since 1995, including more than $15 billion in each of the last two years.[25] Specific commodity subsidies under the current system include those for feed grains ($2.1 billion in 2011); wheat ($1.4 billion); rice ($364 million); upland cotton ($825 million); soybeans ($521 million); peanuts ($77 million); tobacco ($25 million); and dairy products ($30 million).[26] Not all of these subsidies, however, constitute trade-distorting subsidies under WTO rules. For example, only $11.6 billion of $16.3 billion in total U.S. farm subsidies in 2009 constituted "amber box" subsidies (those considered under the WTO Agreement on Agriculture to distort production and trade), and United States reported only $4.3 billion of these to the WTO because of various *de minimis* exclusions—well under its $19.1 billion cap.[27] The current farm bill expires this year and may receive a short-term extension, but it is unlikely that any new farm bill will significantly reduce total agriculture subsidy levels.

Alternative Energy. Since the 1950s, the U.S. government has subsidized the search for, and production of, energy alternatives to fossil fuels, but such funds have expanded dramatically in recent years.[28] The Congressional Budget Office (CBO) estimates that government subsidies to support the production of fuels and energy technologies totaled approximately $24 billion in 2011: $20.5 billion in various tax preferences (special deductions, special tax rates, tax credits, and grants in lieu of tax credits) and $3.5 billion in Department of Energy spending programs (direct investments, primarily for research and development, loans and loan guarantees).[29] The CBO found that 78 percent of all tax subsidies and 54 percent of all DOE subsidies went to alternative energy projects (renewable energy and energy efficiency). Based on DOE's figures, the Institute for Energy Research calculated that fossil fuels (oil, natural gas, and coal) received $0.64 in taxpayer dollars for every megawatt-hour of energy produced, while hydropower received $0.82, nuclear $3.14, wind $56.29, and solar an astonishing $775.64.[30]

Three of the most prominent DOE programs are the Advanced Technology Vehicle Manufacturing (ATVM) program, which aims to improve the energy efficiency of automobiles; the Section 1705 loan-guarantee program, which supports loans for some renewable energy systems, electric power transmission, and biofuel projects; and the Section 1703 loan guarantee program, which aims to increase investment in "clean energy" facilities (primarily nuclear energy). The CBO estimates that the subsidy costs for the ATVM and Section 1705 loan programs between 2009 and 2012 were approximately $4 billion on about $25 billion in loans, although those costs could be higher depending on the economic success or failure of the subsidized firms.

The federal government has also provided a vast array of tax subsidies and other grants to producers and consumers of biofuels such as ethanol, biodiesel, and cellulosic biofuel. According to the U.S. Department of Energy, 538 different federal and state subsidies—grants, tax incentives, loans and leases, rebates, exemptions, and other programs—are currently available to producers or consumers of alternative fuels in the United States. Forty-one of these are federal government programs.[31] The

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CBO estimates that federal excise tax credits for alcohol fuels and for biodiesel alone cost $6.9 billion in 2011.[32] Although some of these subsidies expired in December 2011, many other federal and state subsidy programs continue to funnel billions of taxpayer dollars to U.S. biofuels producers.[33]

Despite some pushback from fiscal conservatives, targeted alternative-energy subsidies continue to have broad bipartisan support. For example, in August 2012 the Senate Finance Committee approved, by a strong bipartisan vote of 19–5, tax extenders legislation containing over $18 billion worth of rebates, credits, and other tax subsidies for alternative energy. A one-year extension of the 2.2-cents-per-kilowatt-hour production tax credit for wind energy alone will cost over $12 billion.[34]

Automobiles. The United States also has a long bipartisan history of subsidizing the domestic auto industry. Most notably, the 2008–09 bailouts of General Motors and Chrysler are projected to cost U.S. taxpayers over $25 billion in direct losses (at current stock prices) and another $20-plus billion in indirect losses (e.g., preferential tax treatment for carryforward of next operating losses).[35] And many experts predict that GM is once again headed for bankruptcy.[36] The bailouts, however, are only the latest example of federal support for Detroit. For example, the Clinton administration, in 1993, provided U.S. automakers with $1.2 billion over eight years to develop hybrid cars as part of its Partnership for a New Generation of Vehicles. The Bush administration's follow-up initiative, FreedomCar, focused on hydrogen-powered cars and cost taxpayers about $2 billion.[37]

The federal government has also doled out extensive consumer subsidies for the purchase of certain vehicles. For example, the 2009 "Cash for Clunkers" program provided government rebates of up to $4,500 for car buyers who traded in their current vehicles for new, more fuel-efficient upgrades, at a total program cost of about $2.8 billion. The Energy Policy Act of 2005 (P.L. 109-58) established tax credits for the purchase of new alternative-fuel and advanced-technology vehicles. Tax credits under this program, expanded by the Emergency Economic Stabilization Act (EESA, P.L. 110-343), are as high as $7,500 for light-duty vehicles and $15,000 for heavy-duty vehicles. General Motors' Chevy Volt qualifies for the maximum $7,500 tax credit—which the Congressional Research Service said is "critical to GM marketing plans for the Volt," given the car's high selling price.[38] The Joint Committee on Taxation estimates that these vehicle subsidies cost $500 million between 2004 and 2008, an estimated $1.3 billion from 2009 to 2013, and another $1 billion in 2014–2015.[39] Many other state programs provide similar consumer subsidies.[40]

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Indictments of U.S. Subsidy Policy

There is ample evidence that the problems caused by subsidies are both real and widespread in the United States. First, U.S. programs have caused significant economic damage. A recent review of the economic literature on federal loan guarantees found that "every loan guarantee program (a) transfers the risk from lenders to taxpayers, (b) is likely to inhibit innovation, and (c) increases the overall cost of borrowing." The paper concluded that, at best, the "guarantees distort crucial market signals that determine where capital should be invested, resulting in lower interest rates that are unmerited and a reduction of capital for more worthy projects. . . . At their worst, these guarantees introduce political incentives into business decisions, creating the conditions for . . . cronyism."[41] The study found that the three main DOE loan programs in particular "fall short of their stated goals of developing clean energy and creating jobs" and cause indirect damage to the nation's economy through "distortion of market signals, cronyism, and mal-investment." Thus, the very public bankruptcies of DOE loan recipients Solyndra, Beacon Power, Ener1, and Abound are more aptly described as a feature, not a bug, of American "green energy" policies. And more green energy failures appear to be on the horizon.[42]

Similar economic harms are caused by other U.S. programs, such as agriculture subsidies, the auto bailouts, and biofuels subsidies. In each case, the costs—via economic distortions, cost overruns, unintended consequences, and cronyism—were found to outweigh any identified benefits. For example, the Cash for Clunkers program was found to cost taxpayers $24,000 per vehicle sold,[43] and the auto bailouts, beyond the financial outlays, were found to constitute a direct and unnecessary payout to the United Autoworkers Union at the expense of taxpayers and investors.[44] U.S. biofuels policies, particularly for corn ethanol,[45] have actually been found to harm the environment, and federal farm subsidies are routinely found to benefit large agribusiness interests at the expense of taxpayers, consumers, and small farmers.[46]

Second, U.S. subsidy policies have created stark political problems, as corruption—or at least the appearance of corruption—is routinely tied to these federal programs. The most famous recent example is the case of U.S. solar firm Solyndra, wherein major contributors to the Obama campaign lobbied for, and received, approximately $500 million in DOE loan guarantees for the soon-to-be-bankrupt company, despite strong evidence of the company's unviability. Solyndra, unfortunately, is not alone: in the recent book, *Throw Them All Out*, author Peter Schweitzer chronicles myriad examples of cronyism and political corruption tied to ever-expanding U.S. subsidy programs. With respect to alternative energy, Schweitzer explains that "the game of funneling taxpayer money to friends has exploded to astonishing levels in recent years."[47] He notes that 71 percent of the Obama Energy Department's grants and loans went to "individuals who were bundlers, members of Obama's National Finance Committee, or large donors to the Democratic Party." These donors together raised $457,834 for President Obama's 2008 campaign, and were subsequently approved for over $11 billion in federal grants or loans.[48] Most recently, Illinois-based energy producer—and Section 1705 loan guarantee recipient—Exelon has been found to have profited handsomely from its cozy relationship with the Obama administration.[49] Such revelations and others led Schweitzer to conclude that "the Department of Energy loan and grant program might be the greatest—and most expensive—example of crony capitalism in American history."[50]

Third, U.S. subsidies also raise serious concerns under international trade rules. The U.S. government's subsidization of specific companies and enterprises subjects U.S. exports—and U.S. trade and subsidy policy more broadly—to scrutiny and potential retaliation by other WTO Members in the form of CVDs or suspended concessions via a WTO dispute. Such responses undermine U.S. efforts to promote trade and to discourage other countries' use of trade-distorting subsidies on the national, bilateral (Free Trade Agreement [FTA]), and multilateral (WTO/G20) levels. They also inject uncertainty into U.S. and global markets, while wasting finite government resources on long legal battles and tit-for-tat trade disputes.

Although many different U.S. exports have been subject to recent anti-subsidy disputes, a few cases and subsidy programs warrant specific mention:

Auto bailouts. In December 2011, the Chinese government imposed antidumping and countervailing duties on U.S. automobile imports. CVDs on imports of Chrysler and GM cars and SUVs were set at 6.2 percent and 12.9 percent, respectively, while all other investigated U.S. automakers received nothing.[51] Among the U.S. subsidy programs alleged in the CVD petition were various elements of the 2009 auto bailouts (including the Automotive Industry Financing Program), the Advanced Technology Vehicles Manufacturing Loan Program, the Cash for Clunkers program, and several federal and Michigan-state tax incentives for U.S. automobile manufacturers and consumers.[52] China's final determination found that Chrysler and GM—but not U.S.-based competitors Ford, Honda, BMW, and Mercedes—had received countervailable subsidies in the form of the auto bailouts via grants, loans, and capital injections. Of particular

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note was China's determination that the two companies were uncreditworthy at the time of receiving U.S. government loans at already-low rates.[53] On July 5, 2012, the United States announced a WTO challenge to various procedural and methodological aspects of China AD/CVD determinations on U.S. automobile imports. However, the United States has not disputed the basis for the Chinese CVD measures—that is, China's assessment that the auto bailout constitutes a countervailable subsidy.[54]

In 2011 American automobile producers exported more than $3 billion of the targeted cars and SUVs to China,[55] but U.S. exports of Chrysler and GM automobiles will remain at a significant price disadvantage until these countervailing duties are removed. Although both companies can avoid the duties by selling cars in China that are produced outside the United States, these duties—imposed because of the auto bailouts—have ensured that their American-based workforce will not reap the benefits of exporting to the largest car market in the world. Such exports also remain vulnerable to similar CVD actions in other key markets.

Meanwhile, the Obama administration has filed a new WTO dispute against the Chinese government, alleging that China's subsidization of domestic automakers and auto parts manufacturers violates WTO rules.[56] Although the legal merits of the United States' allegations are unclear, the audacity of such a move—announced at a campaign rally in Ohio—are beyond question.

Cotton subsidies. In 2004 and again in 2005, the Brazilian government challenged U.S. cotton subsidies at the WTO as violations of the SCM Agreement and the Agriculture Agreement. The WTO's 2005 decision authorized Brazil to retaliate against U.S. goods and services, but Brazil opted instead to allow the United States time to reform its cotton program in line with international trade rules. The U.S. government never did reform the subsidy programs, so Brazil returned to the WTO in 2009 and won permission to impose almost $300 million in retaliatory trade sanctions against U.S. exports. The WTO also opened the door for other retaliatory measures against American patent and other intellectual property rights—a novel approach to addressing noncompliance. Although the U.S. government has not complied with the WTO ruling, Brazil never retaliated because, instead of reforming the program, the United States agreed to provide approximately $140 million in new subsidies to Brazilian cotton farmers.[57] Despite this sordid arrangement, Congress has flatly refused to reform the United States' WTO-illegal cotton subsidy programs, even in the context of a new farm bill. Indeed, Brazil has warned the WTO that it is prepared to retaliate against U.S. exports or by not enforcing U.S. intellectual property rights if the proposed 2012 farm bill takes effect.[58]

Green energy and technology. Perhaps no issue is more indicative of the broader U.S. subsidy debate than federal government support for alternative-energy products. For example, in 2009–2010, subsidized U.S. biodiesel imports became subject to CVD orders in Australia, Peru, and the European Union,[59] while U.S. ethanol subsidies have led to the initiation of trade remedies investigations against U.S. exports in both the EU and China.[60] The Chinese government also has launched two investigations of green-energy subsidies. The first has resulted in a final report showing several instances of "prohibited subsidies" granted by U.S. states, and the Chinese government is now considering whether to bring formal charges to the WTO or take other necessary action.[61] China also has initiated an AD/CVD investigation of U.S. imports of polysilicon—a key component in solar panel manufacturing—alleging that several state and federal subsidies to U.S. renewable-energy producers have injured their Chinese competitors.[62] U.S. producers exported over $397 million worth of polysilicon to China in the first five months of 2012.[63]

Other green subsidy programs also leave U.S. manufacturers vulnerable to future anti-subsidy measures. For example, as explained above, a large majority of all federal loan guarantees under the Section 1705 program have gone to U.S. solar manufacturers.[64] Loan guarantees are expressly listed as a type of "financial contribution" under the SCM Agreement, and a "benefit" will exist to the extent that the amount that the loan recipient pays on the guaranteed loan is less than the "amount that the firm would pay on a comparable commercial loan absent the government guarantee."[65] Given the extremely risky nature of solar lending—a fact highlighted by the CRS and the high-profile failures of government-subsidized firms like Solyndra and Abound Solar[66]—it is all but certain that the Section 1705 loan guarantees have conferred a benefit on U.S. solar producers, and the specificity of this subsidy program to these firms is clear. Thus, the Section 1705 program is very likely a countervailable subsidy. Ironically, the only thing likely preventing a CVD case against U.S. solar panel exports is the green subsidy programs' failure—significant export volumes are needed to cause "injury" in another foreign market, and U.S. solar panel companies remain uncompetitive. U.S. biofuels and polysilicon producers, however, have met with more success, and thus more backlash.

Meanwhile, the U.S. government has launched high-profile CVD investigations of Chinese solar panels and wind turbines, as well as a Section 301 investigation, which allows the president, on his own or via a petition from a private U.S. party, to seek the removal of foreign measures that harm U.S. commerce.[67] The Section 301 investigation of these products led to a WTO complaint against Chinese subsidies to wind-power equipment manufacturers.[68] The solar case alone affects over $3 billion worth of 2011 merchandise trade, and DOC has already announced preliminary affirmative CVD and antidumping determinations. In response to these actions, the Chinese government—no saint when it comes to subsidies and protectionism—immediately deflected criticism by pointing out rampant U.S. subsidies on the same types of products and, as mentioned, by launching its own investigations of U.S. renewable-energy subsidies.

As indicated in Table 1, these trade disputes are part of a broader trend: U.S. exports have increasingly come under anti-subsidy fire since 2008, just as the federal government is pushing to expand U.S. exports under the National Export Initiative and discipline foreign subsidy practices via the new Interagency Trade Enforcement Center (ITEC). Beyond the specific investigations cited, China also has recently imposed CVDs on U.S. steel and chicken parts[69]—both a not-so-subtle response to President Obama's September 2009 decision to impose duties on Chinese tires under Section 421 of U.S. trade law.[70] The U.S. government has, in turn, challenged these measures at the WTO and has been reasonably successful in convincing the trade body that certain of China's procedures violated WTO trade rem-

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Table 1
Global Countervailing Duty Investigations, 2007–2011

	Total CVD initiations	Total U.S. involvement	U.S. as target	U.S. as initiator
2004–2007	33	17	2	15
2008–2011	60	34	7	27
Percent increase (%)	82	100	250	80

Source: World Trade Organization (http://www.wto.org/english/tratop_e/scm_e/scm_e.htm).

edy disciplines. However, much like the autos case, the grounds for these trade investigations—that is, the existence of U.S. subsidies—were not challenged. As more subsidized U.S. exports gain foreign-market share and thereby aggravate domestic competitors, future CVD investigations are seemingly inevitable.

The United States also has been on the losing end of several other high-profile WTO disputes over U.S. subsidies, most notably related to civil aircraft in the Boeing–Airbus dispute. The aircraft cases—one brought by the United States and the other by the European Union—alone implicate tens of billions of dollars in trade, and the WTO has repeatedly found both governments to be guilty of providing WTO-inconsistent subsidies to their domestic manufacturers. Much like the U.S.–China disputes, these matters not only imperil U.S. export opportunities in key foreign markets, but also undermine American calls for subsidy reforms. And, given continuing state and federal subsidization of specific industries, new WTO challenges to these U.S. programs seem inevitable.

Just as the United States has embraced state and federal subsidies for myriad domestic industries, it has sought to limit other nations' use of similar programs through anti-subsidy measures.

U.S. Use of Anti-Subsidy Measures

Just as the United States has embraced state and federal subsidies for myriad domestic industries (increasingly exposing these industries to trade disputes), the U.S. government has sought to limit other nations' use of similar programs through anti-subsidy measures. In fact, the United States has historically been a global leader in the application of CVD measures and has increasingly used them over the last few years. In August 2012, the United States maintained 50 CVD orders on goods from 12 different countries, some dating back to 1986. China is by far the largest target, with 24 CVD orders on Chinese imports beginning in 2007. Nine other CVD investigations are pending covering goods from China, Vietnam, India, South Korea, Oman, and the United Arab Emirates.

The value of imports subject to CVD measures or currently under investigation in 2011 totaled over $11 billion (over $4 billion for goods now under investigation), and 19 CVD orders have been in place for 10 years or more. As a result, U.S. importers and consumers have paid tens of millions of dollars in countervailing duties on these imports over the last several years.[71]

Although that amounts to a rounding error in Washington, these taxes impose real pains on U.S. consumers and tell only a small part of the story with respect to U.S. anti-subsidy policy. First, the data ignore the trade lost or diverted to other sources because of prohibitively high CVDs. Although there are no official government analyses of such effects, the contrast between the per-case import value of pending CVD cases and the much lower values for those for where duties have been imposed provides a strong indication that CVD measures—and their antidumping counterparts—can effectively close off the U.S. market for targeted imports, thus forcing U.S. consumers to pay higher prices for replacement products. Such hidden taxes are impossible to track. Second, the Customs data provide no indication of the indirect economic, legal, and political problems caused by both U.S. anti-subsidy measures and the United States' own trade-distorting subsidy programs.

Criticisms of Existing U.S. CVD Regime

Despite anti-subsidy rules' potential to act as needed checks on domestic and foreign subsidization, the existing U.S. system is problematic and reflects capture by petitioning industries. It is important to remember that, while limiting the proliferation of market-distorting subsidies is a worthwhile endeavor, the remedy is a tax on U.S. consumers—one that can quite literally put them out of business.[72] Extreme care must be taken to ensure that the scope and magnitude of any countervailing duty is as precise as possible, and that the basic WTO disciplines are faithfully applied. Several current DOC policies, however, prevent such application and are intended to expand the scope and size of CVDs well beyond those who are intended to be disciplined and the actual extent of injurious subsidization, respectively. These problems cover broader U.S. policies related to the application of CVDs, as well as specific methodologies for targeting and quantifying countervailable subsidies. The case study on Chinese "policy lending" in the Appendix encompasses many of these concerns.

U.S. application of countervailing duties raises several policy concerns. These problems include inadequate public oversight of, and participation in, U.S. CVD proceedings, a systemic tendency to impose duties in excess of the actual amount of subsidization or injury to the U.S. economy, and diplomatic fallout related to prosecuting foreign companies for allegedly engaging in "unfair" trade.

Countervailing duty determinations by DOC suffer from a lack of transparency that could be easily resolved. DOC has recently enacted a program, IA Access,[73] through which interested parties to a particular AD/CVD investigation and the general public may register with the Import Administration and receive online access to all non-confidential documents filed in U.S. trade remedies proceedings. IA Access is a worthy and long-overdue improvement because for the first time nonlawyers can access and analyze key decisions and public data—particularly those detailing the methodological problems below—without visiting DOC's reading room in Washington, D.C.

However, more could be done improve the overall transparency of the United States' CVD regime. DOC provides little in the way of statistics and other information about previously completed CVD investigations. The existing subsidies library[74] is extremely limited and difficult to navigate, and the previous version was actually superior in terms of navigability.[75] Moreover, no U.S. agency regularly publishes data on U.S. business subsidies or the effects of CVD orders on the U.S. economy. Indeed, the ITC's periodic analysis of the economic effects of U.S. import restraints *specifically excludes* those originating from antidumping or countervailing duty investigations.[76] The only published annual data on AD/CVD duties are collections from Customs, but these only estimate duties paid, not the trade-limiting effects of the measures themselves.[77] As noted above, evidence indicates that such harms are significant.

Countervailing Duties and "Nonmarket Economies"

DOC's current policy, recently affirmed by a new U.S. law,[78] allows for the concurrent application of CVDs and antidumping duties on imports from countries that are designated "non-market economies" (NME) under the U.S. antidumping law (essentially China and Vietnam). This CVD/NME policy results in the imposition of punitive tariffs on imports from NME countries and exposes the United States to continued litigation in U.S. courts and at the WTO. It also demonstrates a dramatic and unnecessary abuse of discretion with respect to Chinese and Vietnamese imports.

The NME methodology is a holdover from the bygone days of command-and-control, Soviet-style economies. Dumping is typically calculated by comparing a foreign exporter's home-market prices with the prices of the same product imported into the United States. Where the former prices are higher than the latter, antidumping duties are imposed on the subject imports in the amount of the difference.

However, for countries designated as NMEs, DOC has ruled that that domestic prices cannot be used to calculate dumping because pervasive government intervention—particularly state subsidies—makes them unreliable. Thus, DOC calculates dumping margins by comparing U.S. import prices with a "price" that has actually been constructed from subsidy-free input costs, expenses, and profits from a comparable producer in a comparable market economy country like India or Thailand (known as "surrogate values"). As a result, the antidumping duty rate on a NME import has little to do with an investigated exporter's actual prices or costs and has already eliminated any possible subsidies that the company received. In fact, DOC, as a matter of policy, uses surrogate values that are free from subsidies.[79]

U.S. application of countervailing duties raises several policy concerns.

Table 2
U.S. Countervailing Duty Investigations, 2007–2011

Country	Product	2011 Value ($)
Orders in Place		
Argentina	Honey	107,159,144
Brazil	Iron Construction Castings	4,115,798
	Carbon and Certain Alloy Steel Wire Rod	96,687,407
	Circular Welded Carbon Quality Steel Pipe	11,416,639
	Certain New Pneumatic Off-Road Tires	210,152,013
	Light-Walled Rectangular Pipe and Tube	392,375
	Laminated Woven Sacks	696,689,482
	Lightweight Thermal Paper	384,938,217
	Raw Flexible Magnets	14,257,532
	Sodium Nitrite	49,865
China	Circular Welded Austenitic Stainless Pressure Pipe	12,727,855
	Circular Welded Carbon Quality Steel Line Pipe	6,816,832
	Citric Acid and Certain Citrate Salts	134,313,619
	Certain Tow-Behind Lawn Groomers and Certain Parts Thereof	238,445,731
	Certain Kitchen Appliance Shelving and Racks	215,325,876
	Oil Country Tubular Goods	26,710,758
	Prestressed Concrete Steel Wire Strand	280,301
	Certain Steel Grating	1,286,009
	Narrow Woven Ribbons with Woven Selvedge	1,604,023,931
	Certain Magnesia Carbon Bricks	51,140,833
	Certain Seamless Carbon and Alloy Steel Standard, Line, and Pressure Pipe	95,447,726
	Certain Coated Paper Suitable for High-Quality Print Graphics	61,331,026
	Certain Potassium Phosphate Salts	6,445,440
	Drill Pipe	192,735,223
	Aluminum Extrusions	1,159,723,201
	Multilayered Wood Flooring	733,115,975
	High Pressure Steel Cylinders	81,665,660
India	Sulfanilic Acid	2,550
	Certain Cut-to-Length Carbon Quality Steel Plate	2,500,516
	Certain Hot-Rolled Carbon Steel Flat Products	14,616,034
	Polyethylene Terephthalate Film, Sheet, and Strip (PET Film)	50,906,367
	Prestressed Concrete Steel Wire Strand	-
	Carbazole Violet Pigment 23	1,958,387
	Certain Lined Paper Products	4,940,171
	Commodity Matchbooks	1,483,602

Table 2 ***Continued***

County	Product	2011 Value ($)
Orders in Place		
Indonesia	Certain Cut-to-Length Carbon Quality Steel	-
	Certain Hot-Rolled Carbon Steel Flat Products	-
	Certain Lined Paper Products	2,824,777
	Certain Coated Paper Suitable for High-Quality Print	18,535,104
Iran	In-Shell Pistachio Nuts	–
	Roasted In-Shell Pistachios	-
Italy	Certain Pasta	173,328,336
	Certain Cut-to-Length Carbon Quality Steel Plate	116,601,027
Republic of Korea	Corrosion-Resistant Carbon Steel Flat Products	138,078,076
	Stainless Steel Sheet and Strip in Coils	65,296,052
South Africa	Stainless Steel Plate in Coils	266,457
Thailand	Certain Hot-Rolled Carbon Steel Flat Products	1,006,707
	Welded Carbon Steel Standard Pipe	28,270,387
Turkey	Certain Pasta	992,165
Pending Investigations		
China	Drawn Stainless Steel Sinks	117,949,508
	Crystalline Silicon Photovoltaic Cells	3,145,091,228
	Utility Scale Wind Towers	222,084,864
India	Circular Welded Carbon-Quality Steel Pipe	64,572,001
Oman	Circular Welded Carbon-Quality Steel Pipe	28,082,038
Republic of Korea	Large Residential Washers	568,584,577
United Arab Emirates	Circular Welded Carbon-Quality Steel Pipe	53,929,405
Viet Nam	Circular Welded Carbon-Quality Steel Pipe	50,116,747
	Polyethylene Retail Carrier Bags	370,286
	Steel Wire Garment Hangers	31,980,556
	Total In Place	**6,769,371,469**
	Total Pending	**4,282,390,924**
	Total Orders	**11,051,762,393**

Source: Author's calculations from ITC Dataweb, DOC notifications and December 31, 2011, notification to the WTO (http://docsonline.wto.org/DDFDocuments/t/G/SCM/N235USA.doc).

Given DOC's questionable and incongruous reasoning, it is unsurprising that Chinese exporters and the Chinese government challenged the agency's policy change in U.S. courts and at the WTO.

As already discussed, CVDs are intended to offset subsidies and thus to ensure that U.S. producers have a "level playing field" against subsidized foreign competition. They are often imposed concurrently with antidumping duties on market economy imports, but only in 2007 did DOC decide that it could impose CVDs on NME imports that also were subject to antidumping duties—a stark and unexpected reversal of its decades-old policy against such concurrent application, precisely because pervasive government intervention in NMEs precluded the proper measurement of a subsidy's size and effect. Since that reversal, the United States government has issued 24 final CVD orders on goods from China, 1 for Vietnam, and 5 other CVD investigations of goods from these countries (3 from China and 2 from Vietnam) are now pending (see Table 2).

DOC's reversal created a fundamental conflict between the agency's views on China in the antidumping and CVD contexts. In antidumping cases, DOC maintained its long-standing view that the Chinese government's economic interventions so distorted prices and costs that a standard market economy methodology was impossible. In the latter context, however, DOC suddenly found that economic reforms in China made domestic prices and costs *just reliable enough to* permit the measurement of subsidies and specificity (and thus the application of the U.S. CVD law to Chinese imports).

Moreover, DOC's policy reversal revealed the abundant discretion that it has with respect to NME decisions. In issuing memoranda in two separate investigations only a few months apart—an August 2006 NME memorandum in an antidumping investigation of Chinese lined paper[80] and a March 2007 memorandum reversing previous policy (announced in the *Georgetown Steel* case) in the first CVD investigation of Chinese coated paper[81]—DOC used the same evidence to come to precisely the opposite conclusions about the Chinese economy. In both cases, DOC examined the macroeconomic factors that are required for an NME analysis under U.S. law (currency, wages, investment, state ownership, government control over production and prices, and other factors) and made the following findings:

- In the NME Memorandum, DOC concluded that China is no longer a Soviet-style command economy, but remains an NME for purposes of the U.S. antidumping law. DOC found that China "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."
- In the *Georgetown Steel* memorandum, DOC concluded that China is "significantly different" and "more flexible" than a Soviet-style economy, and thus may be subject to the U.S. CVD law. DOC found that "it is possible to determine whether the 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."

Thus, in the span of only seven months and using the exact same evidence, DOC concluded that China is no longer a Soviet-style economy and that prices and costs are too unreliable for the purposes of determining the fair market value of merchandise but, prices and costs are sufficiently reliable for the identification and quantification of a subsidy benefit.[82]

Given DOC's questionable and incongruous reasoning, it is unsurprising that Chinese exporters and the Chinese government challenged the agency's policy change in U.S. courts and at the WTO. In so doing, the parties argued that the simultaneous application of antidumping and countervailing duties on NME imports violated U.S. law and WTO rules because, among other things, the duties were artificially high because they offset the subsidies twice—a process known as "double counting." The WTO Appellate Body agreed with China and has directed the United States to develop a new methodology which protects against double counting for the four CVD investigations that were at issue in that dispute. A lower court in *GPX International Tire v. United States* twice came to a similar conclusion as the WTO, but on appeal the U.S. Court of Appeals for the Federal Circuit went much further, ruling that Commerce's long-standing policy had been tacitly ratified by Congress, and thus the U.S. CVD law cannot apply to NME imports unless and until Congress expressly revises the law to state as much.

The court's ruling invalidated the White House's primary approach to countering Chinese subsidies—a pillar of the president's trade-enforcement policy. In a joint letter to the Senate Finance and House Ways and Means Committee, U.S. Trade Representative Ron Kirk and then–Commerce secretary John Bryson pleaded with Congress to quickly pass legislation applying the CVD law to NME imports. After only 32 minutes of House debate and none in the Senate, Congress willingly complied with the administration's request, and on March 6, 2012, passed legislation that allowed the Obama administration to continue its CVD/NME policy in the pending investigations of NME imports and all future cases retroactively applied U.S. CVD law to dozens of completed CVD investigations of NME imports, and only prospectively (i.e., from the date of signing) authorized DOC to address double-counting. President Obama signed the CVD/NME bill into law one week later.

The U.S. government's CVD/NME "fix" will unfortunately create as many problems as it solves. First, the retroactive application of the revised CVD law to existing duties will lead to more litigation and uncertainty, as aggrieved parties try to recover the millions of dollars in duties that the U.S. government had no lawful authority to impose or collect. Such litigation has already started in the U.S. courts as the CAFC remanded the original *GPX* case to the lower Court of International Trade (CIT) for a ruling on the CVD/NME law's constitutionality,[83] and another Chinese firm has since raised similar constitutional arguments in a new CIT appeal.[84] Moreover, the Chinese government has unsurprisingly challenged the DOC's identical, WTO-inconsistent use of double counting in the 20 other completed cases that had not yet been the subject of WTO dispute settlement. (As noted below, those CVD investigations, and a few others, are also the subject of a new WTO dispute on other grounds.)

Second, the legislative fix will do little to resolve the myriad problems that existing U.S. practice creates. Most notably, "double counting"—a problem that, according to DOC itself, would be difficult, if not impossible, to truly solve—will continue in some form, thereby unfairly penalizing U.S. consumers of Chinese and Vietnamese imports, while subjecting the United States to further litigation and exposing U.S. exporters to WTO-sanctioned retaliation because of noncompliance. Indeed, DOC's first attempt to comply with the new law's double-counting provisions has resulted in a half-measure that addresses only a small fraction of the subsidies found to have been utilized by foreign exporters in the underlying investigations. As a result, DOC's ad hoc methodology does not capture all instances of double counting and does very little to limit the punitive damage inflicted on U.S. importers because of the agency's existing CVD/NME policy.[85]

Third, continuing the existing policy furthers harm U.S.-China trade relations and needlessly keeps the United States on the defensive in bilateral negotiations. The administration has many legitimate complaints against unfair or distortive Chinese trade practices, but the CVD/NME issue—and the United States' continued refusal to comply with adverse court and WTO rulings—undermines the strength of those very valid concerns. As a result, U.S. recalcitrance harms other, more important negotiating objectives, such as improving China's enforcement of intellectual property rights.

Given these problems, it is clear that this policy should end.

Injury Analysis

As with antidumping investigations, the injury portion of a CVD investigation contains several flaws that harm U.S. consumers and subvert the remedial intent of U.S. trade law. First, the law precludes the U.S. International

The administration has many legitimate complaints against unfair or distortive Chinese trade practices, but the CVD/NME issue—and the United States' continued refusal to comply with adverse court and WTO rulings—undermines the strength of those very valid concerns.

The United States' application of CVDs on foreign imports also raises serious methodological concerns. As a result, U.S. CVD measures have been subject to 21 WTO complaints since 1997.

Trade Commission from considering the interests of consumers or consuming industries, or whether the imposition of CVDs is in the greater public interest, when considering the effects of import duties. As a result, CVD investigations may be initiated—and duties may be imposed—even where such cases overwhelmingly harm the U.S. economy.

Second, unlike some governments that formally recognize the ill effects of duties on the domestic economy, the United States does not apply a "lesser duty rule," which would give discretion to the authorities to apply a lower duty rate than the one calculated by the Commerce Department if that lower rate were considered sufficient to remedy the injury. Instead, the CVDs imposed are frequently far in excess of the level necessary to prevent particular U.S. companies and workers from being harmed by subsidized foreign competition.

Finally, U.S. law grants a domestic-company standing to bring a CVD case against imports from a certain country or countries, even where that company imports a significant portion of like products from third countries. As a result, U.S. companies can use countervailing duties (and antidumping duties) to give their preferred import sources a government-created competitive advantage in the U.S. market versus other foreign competitors.[86] Such strategy subverts the intent of U.S. trade laws, which is to cure injury to domestic industries and workers caused by certain imports.

The United States' application of CVDs on foreign imports also raises serious methodological concerns. As a result, U.S. CVD measures have been subject to 21 WTO complaints since 1997. Most recently, U.S. CVD policy has been the subject of three high-profile disputes filed by China and one from India.[87] China won on several issues (including the United States' improper categorization of certain state-owned entities as "public bodies" and, as noted above, double counting) in the first dispute and has raised similar claims in its two subsequent challenges, which is in the early stages and covers dozens of CVD investigations, including pending ones on Chinese solar panels and wind towers. On July 12, 2012, India requested the formation of a WTO dispute settlement panel to adjudicate its claims against several aspects of U.S. CVD law and practice,[88] and that panel was established on August 31, 2012. Each of these disputes challenges the WTO-consistency of many of the methodological issues discussed in the following sections.

Consultations with Foreign Governments

U.S. law and WTO rules require the United States government to notify the home government of an exporter named in a petition and to provide "an opportunity for consultations" with respect to the petition prior to the initiation of the investigation.[89] However, these consultations rarely, if ever, prevent or delay DOC's initiation of a CVD investigation or resolve the dispute, even though they are intended, as noted in the SCM Agreement, to "clarify the situation . . . and arriv[e] at a mutually agreed solution."[90] Indeed, in the recent administrative review of *Hot-Rolled Carbon Steel Flat Products from India*, the Indian government claimed a due-process violation because there had been no bilateral consultations prior to DOC investigation of newly alleged subsidy programs. DOC rejected India's claim, stating that U.S. law contained no such requirement and DOC was not bound by WTO rules.[91]

Public Body

As noted above, a financial contribution may be provided by a government or public body, or a private body that is entrusted or directed by the government to do so. DOC historically treated any state-owned entity as a public body and thus as the government itself. However, the WTO Appellate Body, in a landmark 2010 decision, found DOC's interpretation to be erroneous and instead confirmed that a public body was an entity that possesses, exercises or is vested with governmental authority, which is essentially the power to make or administer government laws, regulations, or policies. DOC was supposed to revise its public body standard in response to the Appellate Body's decision, but has so far refused. In the investigations underlying the

WTO dispute, DOC's "new" policy still emphasizes state ownership and control over an entity rather than the entity's possession and exercise of powers typically vested in a government.[92] And in all other investigations, DOC still uses its old standard, even in proceedings that began well after DOC's public body standard was rebuked at the WTO.[93] In response to this recalcitrance, China has again challenged DOC's public body standard at the WTO, filing the complaint only days after DOC issued its revised policy.[94]

Although one could argue that a broad public body definition is preferable from a free market economic perspective because it discourages government-owned enterprises, this view ignores reality and the law. First, many developing countries remain heavily invested in commercial enterprises, and such a standard would discourage them from supporting global trade rules and pursuing privatization efforts that are consistent with their stage of development. Second, a broad standard is plainly inconsistent with the views of the Appellate Body, which are firmly based on the agreed text of the SCM Agreement. Such a standard invites trade litigation, which results in additional market uncertainty and diminished U.S. legitimacy. Finally, a broad public body standard is wholly unnecessary because DOC or another administering authority (or a WTO panel) may still countervail the actions of a nonpublic body where it finds that the entity has been entrusted or directed by the government to provide a subsidy. That DOC simply does not wish to undertake this additional step—one that would likely be fulfilled by the same evidence of state ownership and control that DOC now uses to find a public body—is not sufficient grounds for ignoring it.

Measuring Subsidies and Benchmarks

Existing U.S. law gives DOC ample discretion to measure the benefit (and thus the magnitude) of an alleged subsidy, including the use of external subsidy benchmarks that have no relation to the domestic market at issue. This can lead to the imposition of CVDs that exceed the actual level of subsidization in the market and thus penalize U.S. importers and consumers rather than offset the injurious subsidies at issue. As noted above, in cases of grants or tax breaks, the calculation of benefits is straightforward—it is the amount of the grant or the tax revenue forgone. However, in many other cases (particularly for government-provided loans, goods, or services), DOC resorts to external benchmarks from other markets or world-market prices, where it determines that domestic interest rates or prices—the preferred benchmark—are unusable. These benchmarks often have little to do with the unique comparative advantages of the domestic market at issue and are expressly preferred over constructed benchmarks (e.g., cost of production plus profit) based on prevailing market conditions in the country of provision.[95]

As a result of this policy, DOC has used external benchmarks to determine the magnitude of many subsidies, including those related to government-provided loans, land, water, stumpage (wood), and metals. The calculations resulting from DOC's use of external benchmarks have produced subsidy amounts that often have very little to do with the market value of the actual government-provided loan or good/service at issue and negate the investigated countries' natural comparative advantages. Thus, final CVD rates for these subsidies are often much larger than the actual benefit, if any, that an exporter has received from the government transaction.

DOC's recent CVD investigation of aluminum extrusions from China provides an example of the difficulties involved with external benchmarks. In that case, DOC used prices for raw aluminum from the London Metal Exchange and prices for land from Thailand, rather than in-country prices for these goods.[96] Although one could reasonably argue that London Metal Exchange aluminum prices are roughly comparable to those in China because aluminum is a globally traded commodity, no such reason applies for something so uniquely country-specific as land. Thus, any "land subsidy" found to exist in this case has little relationship to the actual subsidy, if any, conferred by the Chinese government.

Existing U.S. law gives DOC ample discretion to measure the benefit (and thus the magnitude) of an alleged subsidy, including the use of external subsidy benchmarks that have no relation to the domestic market at issue.

DOC's interpretation of specificity dramatically expands the scope of U.S. CVD law—and DOC's discretion under it—to discipline many types of routine economic regulation and/or broadly available subsidies.

Legislative proposals to address "currency misalignment" would exacerbate existing concerns because they would authorize DOC to calculate the amount of a currency's undervaluation by using a basket of other comparable countries' currencies as a surrogate for what that currency's value should actually be in an uncontrolled market. Such a market benchmark would not reflect the many unique circumstances surrounding the value of a nation's currency. Moreover, because such legislation is not limited to China (such limitation would violate WTO non-discrimination rules) and because many other countries engage in similar forms of currency management, currency/CVD proposals would open the door to copycat cases against imports from many countries other than China. For example, a recent study by the Peterson Institute alleged that counties like Switzerland, Malaysia, Algeria, Russia, and others engage in "currency manipulation."[97] Should a currency/CVD proposal become law, there would be nothing to stop domestic industries and unions—and their lawyers—from pursuing CVD cases against all of these countries, using external subsidy benchmarks to find a benefit where none might actually exist.

Specificity

Existing DOC practice allows for a finding of specificity under several dubious conditions. For example, a subsidy may be found to be specific where only one subsidy element—financial contribution or benefit—is limited to an investigated industry or enterprise. Although this approach might appear harmless, or even a helpful way to ensure that all subsidies are disciplined, it actually raises serious legal and practical concerns. First, both U.S. law and the SCM Agreement make clear that only a specific subsidy—as defined under the law as *both* a financial contribution and a benefit—may be countervailed. There is no rule allowing for partial specificity.

More importantly, DOC's interpretation of specificity dramatically expands the scope of U.S. CVD law—and DOC's discretion under it—to discipline many types of routine economic regulation and/or broadly available subsidies. For example, under DOC's specificity standard, a basic tax deduction, although unlimited (i.e., available to all domestic industries and individuals), could be found to be a de jure specific subsidy to the steel industry, where the government at issue has simply expressed through official documentation a desire to support domestic steelmakers through the tax code. Under such circumstances, the industry has received no preferential treatment from the government when compared with other domestic industries, yet somehow it has received specific—and thus countervailable—subsidies. This result is precisely what the specificity standard was originally designed to guard against, and, if widely copied, DOC's broad specificity standard could undermine the SCM Agreement's delicate balance and thus deter WTO Members from adhering to the subsidy disciplines that they have voluntarily agreed to follow.

Attribution

Existing DOC practice allows the agency to attribute to investigated foreign exporters subsidies received by the firms' "cross-owned" affiliates, including upstream input producers, even though the affiliation is loose (e.g., has a significant, but not majority, shareholding by a common parent) an affiliated producer has not produced the subject merchandise, but merely has the potential to do so; or there's no evidence on the investigation record that an affiliated input-producer's inputs have been used in the downstream product that is then exported to the United States. This practice leads to situations in which investigated exporters are responsible for subsidies received by perhaps dozens of loosely affiliated companies that they don't know and can't control—subsidies that had no impact on the U.S. market for the downstream product at issue. As a result, final duties paid by U.S. importers can be much higher than the actual level of subsidies received by investigated foreign exporters, and thus higher than the actual level of trade distortion.

Key elements of DOC's attribution standards, as set forth in its regulations,[98] are as follows:

Cross-ownership: Cross-ownership exists between two or more corporations where one corporation can use or direct the individual assets of the other corporation(s) in essentially the same ways it can use its own assets. This standard will normally be met where there is a majority voting interest between two corporations, or through common ownership of two (or more) corporations. The Court of International Trade (CIT) has upheld the DOC's authority to attribute subsidies based on whether a company could use or direct the subsidy benefits of another company in essentially the same way it could use its own subsidy benefits.[99] However, the standard is met even where there is no majority voting ownership interest between, or common ownership of, the corporations at issue.

Cross-owned Producers: Subsidies received by a cross-owned corporation may be attributed to the affiliated subject exporter where the former corporation merely has the ability to produce the subject merchandise. Actual production is not required.[100]

Cross-owned Input Producers: Subsidies received by a cross-owned input producer may be attributed to a downstream-subject exporter where the input producer's merchandise could theoretically be used to produce the subject merchandise exported to the United States. Actual use in such merchandise is not required, and a showing that the input was not used in such merchandise is immaterial. Only a showing that the input cannot be used (e.g., by statute or physical impossibility) would overcome the standard. It is unclear why this provision even exists, given that U.S. law and the DOC regulations have specific provisions allowing for the investigation and countervailing of upstream subsidies provided via input producers.[101]

The policy lending case study in the Appendix shows the extent to which these attribution standards can result in CVDs that have little connection to the actual merchandise being imported into the United States.

Reform Proposals

Global anti-subsidy rules and the U.S. countervailing duty law have a legitimate role in discouraging both injurious foreign-subsidy practices and the seemingly unstoppable political inertia behind America's subsidy addiction. But clearly the current U.S. system is far from ideal. If the U.S. countervailing duty law is ever to earn the support of free-market advocates and become a positive policy tool for subsidy reform efforts, the U.S. government must enact several policy and methodological improvements. Given the current gridlock in Washington, it is important to note that many of these reforms would not require new laws or an act of Congress, and instead could be carried out via administrative rulemaking or simple changes in existing executive-branch policy.

Reform or Eliminate U.S. Subsidy Programs

Current U.S. subsidy policies not only are economically and politically problematic but also raise serious legal concerns and undermine U.S. trade interests. The U.S. government should conduct a top-to-bottom review of all subsidy programs, particularly farm subsidies and those for "green" energy and technology, to determine whether they comply with global trade rules. Those that are specific to certain industries or prohibited (i.e., contingent upon exportation or the use of domestic versus imported goods) should be eliminated. This change would allow the U.S. government to continue to provide broad-based economic incentives—for example, for research and development or general infrastructure—while limiting potential legal concerns at the WTO or in foreign export markets, or in U.S. trade negotiations due to allegations of countervailable subsidies. As an added benefit, this reform would get the United States government out of the business of picking winners and losers, as well as limiting distortions to the domestic economy and international trade flows caused by the U.S. government's economic adventurism. Similar reforms should be encouraged at the state and local level.

The U.S. government should conduct a top-to-bottom review of all subsidy programs, particularly farm subsidies and those for "green" energy and technology, to determine whether they comply with global trade rules.

A conclusion by the Department of Commerce that China or Vietnam is a market economy under the U.S. antidumping law would have no legal or economic repercussions outside of the trade-law context, and would thus in no way affect the United States' ability to promote economic reforms in these countries.

Improve Subsidy-Related Transparency

In order to improve transparency and foment a more informed debate about U.S. subsidy policy, DOC should improve its database of countervailable/noncountervailable subsidies in order to help U.S. producers, importers, and consumers better understand foreign subsidy practices and the department's treatment of them. Moreover, DOC and the ITC should engage in a more thorough public accounting of the costs of U.S. subsidies and of new CVDs, and should publish an annual report on the magnitude of U.S. subsidy programs, broken down by industry; CVDs collected from (i.e., taxes imposed on) U.S. importers because of existing orders, as well as the estimated economic loss caused by such duties; the health of the domestic industries protected by CVDs; and any trade diversion—that is, any shift in imports from targeted countries to other markets that are not subject to CVD orders—caused by anti-subsidy measures. Such a report could be requested by the White House or Congress under Section 332 of U.S. law.

End the CVD/NME Policy

The U.S. government should terminate its existing CVD/NME policy by implementing one of two alternatives: graduate China and Vietnam to market-economy status and apply the standard antidumping methodology, or repeal the CVD/NME law and apply only the NME methodology in antidumping cases.

Contrary to some misperceptions, a conclusion by DOC that China or Vietnam is a market economy under the U.S. antidumping law would have no legal or economic repercussions outside of the trade-law context, and would thus in no way affect the United States' ability to promote economic reforms in these countries. Moreover, DOC has ample discretion as to whether to designate a country a market economy or a non-market economy.[102] It is required by law to analyze the six factors provided by law, but its conclusions with respect to each factor, and the country's status overall, are discretionary. It is this discretion that allowed DOC to designate Russia a market economy in 2002, even though that country only became a WTO Member this year.

On the other hand, such graduation would have many benefits. First, and most obviously, it would effectively end the use of DOC's problematic NME methodology, which, as documented in another Cato Institute paper, is arbitrary, opaque, and punitive.[103] This would allow antidumping investigations of Chinese and Vietnamese imports to become more predictable and transparent—a boon to U.S. importers and consumers who need to make long-term sourcing decisions. Second, NME graduation would quell the domestic and international litigation surrounding DOC's current policy, including the ongoing constitutional challenges to the new CVD/NME law and WTO dispute settlement compliance proceedings. This would allow DOC to continue to apply CVDs to Chinese and Vietnamese imports without the constant threat that U.S. courts or the WTO will again rule that DOC's practice violates U.S law or global trade rules, respectively.

Third, and related, NME graduation could improve U.S. relations with China and Vietnam and help bilateral negotiations on important issues like intellectual property rights, services liberalization, export restraints, and state-owned enterprises. As argued in a 2009 Cato Institute paper with respect to China's NME status:

> Graduation from NME status is one of the Chinese government's top international trade priorities. China wants to be treated like all other major economies, and accordingly, the Chinese government is likely willing to make important concessions in other contested areas of trade policy to achieve market economy status. But the longer we wait to grant market economy status to China, the less valuable that concession becomes. Under the rules governing China's accession to the WTO, the United States must repeal China's NME designation by 2016. Thus, the value of that "concession" will be greater in 2009—seven years early—than it will be in 2010 or 2012.[104]

Vietnam has a similar requirement in its WTO accession agreement, effectively terminating the United States' use of the NME methodology for Vietnamese imports on December 31, 2018.[105] Of course, the passage of time, and the ongoing uncertainty surrounding the legality of the U.S. CVD/NME policy, have reduced the value of the United States' NME negotiating chips, but they still might prove to be useful carrots in bilateral negotiations. For example, Vietnam has expressed a strong desire to terminate the application of the NME methodology by all participants in the Trans-Pacific Partnership trade negotiations, including the United States.[106] China also still views NME graduation as one of its top trade priorities, as its continued litigation of NME-related issues in the United States and elsewhere makes clear.[107]

The other alternative is to repeal the CVD/NME law and apply only the NME methodology in antidumping cases. Every CVD order imposed on imports from China and Vietnam has been accompanied by an antidumping order on the same product and, as noted above, the NME methodology already offsets any subsidies received by an investigated foreign producer/exporter.[108] Thus, the U.S. government could continue to address Chinese subsidies via the NME antidumping methodology and simply not apply CVDs to NME imports. However, the new CVD/NME law might make this alternative more difficult because repeal is highly unlikely.

Require Meaningful, Transparent Consultations

As noted above, prior initiating a CVD investigation, the United States is required by U.S. law and WTO rules to invite the subsidizing government(s) listed in a CVD petition for consultations to resolve the dispute. These consultations, however, often do not occur or are ineffective when they do, even though the pre-initiation resolution of a subsidy dispute could eliminate the costs associated with a CVD investigation and final duties and even result in the termination of the foreign subsidies at issue. Thus, the United States should amend DOC's regulations[109] to require the government to enter into such consultations (rather than merely "invite" the government do so) during the 20-day initiation period; notify all interested parties of such consultations and solicit comments thereon,[110] and publish the other government's rejection of the U.S. consultations request or a transcript of the consultations and the reasons for their outcome. The government also should amend U.S. law[111] to extend the consultations requirement to newly initiated subsidy programs, particularly in annual reviews, and allow DOC to extend the 20-day time period for initiating a CVD investigation where bilateral consultations are ongoing and not initiate the case where the consultations produce a mutually satisfactory resolution.

Utilize a WTO-Consistent "Public Body" Standard

DOC's current standard for identifying "public bodies" is a plain violation of global trade rules and invites litigation and potential retaliation against U.S. exports. Thus, the DOC should revise its public body standard to adhere to the WTO's "governmental authority" test and should use the "entrustment or direction" provision for any state-owned enterprises that do not possess such authority. This change would conform DOC's definition to global trade rules and alleviate needless litigation over the current approach, while retaining the necessary scrutiny of the transactions of foreign state-owned enterprises. It would require no changes to U.S. law or regulations.

Use External Benchmarks Only as a Last Resort

DOC's regulations contain a preference for world-market prices where domestic prices are found to be unusable. The department should amend its regulations[112] to establish an affirmative burden on DOC to demonstrate, based on positive evidence, that domestic prices or interest rates are not "useable" by DOC to calculate a subsidy benefit, and where that burden is met, require DOC to determine benefit based on a cost-based benchmark,

The U.S. government should continue to resist any expansions of the CVD law to cover national currency practices.

rather than world-market prices. And where world-market benchmarks must be used, the amendments should require DOC to adjust them based on the unique market characteristics of the investigated country—or demonstrate, with positive evidence—that such adjustments are unnecessary.

More broadly, the U.S. government should continue to resist any expansions of the CVD law to cover national currency practices because these would inevitably require the construction of a "currency benchmark" that has little relation to the nation at issue and is ripe for abuse by opportunistic domestic industries and their congressional representatives that are eager to thwart global competition.

Tighten Standards for Specificity

As explained above and in the policy lending case study, DOC's current specificity standard allows for illogical and unfounded conclusions with respect to whether a subsidy is specific to certain enterprises or whether it exists at all. Thus, DOC should reform its specificity standard such that a subsidy will only be found to be specific where both the financial contribution and the benefits derived therefrom are specific to certain enterprises or industries.

This change would not only be consistent with the intent and language of the SCM Agreement but also would ensure that specific subsidies remain subject to remedial measures and thus would be discouraged. Policy lending, for example, could still be found to constitute a countervailable subsidy under this revised standard, where DOC establishes that the Chinese government had explicitly targeted a certain enterprise for a preferential allocation of state-provided loans and that the targeted enterprise was explicitly scheduled to receive more loans than similar enterprises that were not targeted by the government (or that the firm otherwise would have received in the absence of the government program). And, of course, a specific subsidy would exist where the government explicitly required banks to provide loans to certain favored industries at discounted rates (or evidence showed that these firms received such rates). In both cases, there is an explicit, specific financial contribution and an explicit, specific benefit.

On the other hand, broadly available government policies—such as government-set or government-influenced interest rates—would not result in CVDs when certain officials merely announced their preference for a certain industry. Indeed, it would not be difficult to imagine a situation where a U.S. bank with a significant percentage of government ownership was alleged to have provided government loan subsidies to a solar manufacturer because of the Obama administration's stated preference for the domestic solar industry and the Federal Reserve's influence over lending rates via the federal funds rate.

It would not be difficult to imagine a U.S. bank with a significant percentage of government ownership providing government loan subsidies to a domestic industry based on the administration's stated preference and the Federal Reserve's influence over lending rates.

Reform Attribution Standards

DOC should revise its regulations on attribution[113] to ensure that cross-ownership will not apply in any cases where there is less than a majority voting interest between two firms or through a common parent company. Furthermore, DOC may only attribute subsidies received by a cross-owned input producer where it has proven, on the basis of positive evidence, that the producer's inputs have actually been delivered to the investigated exporter, or, alternatively, DOC could eliminate the provision altogether and use only the "upstream subsidy" regulations.[114] These changes would preclude DOC from assigning to investigated exporters subsidies received by loosely affiliated input producers whose subsidized inputs were never—but theoretically could be—used by the investigated exporter. As such, the change would allow DOC to more accurately estimate the extent to which an investigated import has been subsidized (and thus distorts the U.S. market) and would help prevent punitive CVD rates.

Revise Injury Standards

Policymakers should revise the CVD law to allow the International Trade Commission to consider the public interest and consumer interests when initiating cases and determining whether subsidized imports have caused material injury. U.S. law should also be revised to include the lesser duty rule and to prevent domestic industries from qualifying as petitioners where they or their affiliates import significant volumes of the subject merchandise from third countries.

Conclusion

National and multilateral disciplines on subsidies can play an important role in curtailing the explosion of global subsidies and limiting the economic and political damage caused by targeted state support for favored industries. Without them, policymakers at home and abroad will continue to funnel public monies into their chosen industries while blaming each other for such misbehavior. Unfortunately, the United States is in no position to lead any global reform efforts because its "do as I say, not as I do" approach to domestic and foreign subsidies undermines its credibility. While decrying foreign governments' industrial subsidization, the U.S. government annually provides almost $100 billion in direct and indirect subsidies to U.S. businesses—subsidies that have been repeatedly found to distort global markets, strain the federal budget, breed cronyism, and undermine public support for our political system and the free market. Many of these subsidies also violate global trade rules and, as a result, are increasingly subject to anti-subsidy measures at the WTO and in important foreign markets.

Moreover, the federal government's application of the U.S. countervailing duty law reflects capture by domestic industries, diverges from multilateral anti-subsidy principles, and imposes taxes on U.S. consumers that well exceed those necessary to remedy foreign governments' injurious subsidization. As a result, the U.S. government is embroiled in domestic and international disputes that undermine market certainty and harm U.S. commercial and foreign policy interests.

A better approach is possible—one that maintains pressure on foreign subsidy practices while restoring American legitimacy, discouraging political pandering, improving the economy, and bolstering public support for free-market democracy. This approach would make U.S. subsidy policies conform to global trade rules and reflect a more limited, economically justifiable, and commonsense approach to government incentives, and it would ensure that the U.S. CVD law is truly remedial, rather than protectionist and WTO-inconsistent. Indeed, if U.S. policymakers want to turn the United States into a global export powerhouse, they should start with removing U.S. exports' vulnerability to competitiveness-killing CVDs or WTO-sanctioned retaliation due to rampant industrial subsidization and the misapplication of the U.S. CVD law. Should the U.S. government continue to eschew such reforms, the global solar panels debacle promises to be only the tip of the iceberg.

Should the U.S. government continue to eschew reforms to countervailing duty laws or limit damage to U.S. exports through World Trade Organization–sanctioned retaliation, the global solar panels debacle promises to be only the tip of the iceberg.

Appendix
Case Study: Chinese Policy Lending

DOC's conclusions with respect to the countervailability of loans from state-owned commercial banks—that is, "policy lending" in China, provides a perfect example of many of the policy and methodological problems outlined in this paper. DOC recently described its framework for determining whether this program constitutes a countervailable subsidy by the government of China (in the department's terms, "GOC") in the investigation of *Steel Wheels from China*, as follows:

> [T]he Department looks to whether government plans or other policy directives lay out objectives or goals for developing the industry and call for lending to support those objectives or goals. Where such plans or policy directives exist, then it is the department's practice to determine that a policy lending program exists that is specific to the named industry (or producers that fall under that industry). Once that finding is made, the department relies upon the analysis undertaken in [the 2007 case of *Coated Free Sheet Paper from China*] to further conclude that national and local government control over the [state-owned commercial banks] results in the loans being a financial contribution by the GOC. Therefore, on the basis of the record information described above, we determine that the GOC has a policy in place to encourage the development of the automobile industry, including the production of auto parts, through policy lending. . . .
>
> [W]e determine that the lending constitutes a direct financial contribution from the government . . . , and they provide a benefit equal to the difference between what the recipients paid on their loans and the amount they would have paid on comparable commercial loans. . . . We determine that the loans are de jure specific . . . because of the GOC's policy, as illustrated in the government plans and directives, to encourage and support the growth and development of the automotive and auto parts industry, including producers of steel wheels.[115]

In short, the department's analysis concluded that a policy lending program for a certain industry exists wherever government documents indicate that the Chinese government has expressed support for providing loans to a particular industry. State-owned banks in China constitute public bodies because they are owned and controlled by the Chinese government, so the banks' loans to the industry under investigation automatically qualify as government loans and are thus financial contributions. These loans confer a benefit to the extent that they are provided at interest rates that are lower than comparable commercial rates. Finally, the loans are de jure specific because of the aforementioned government statements in support of the industry.

DOC has utilized an identical analytical framework in a majority of the CVD investigations of Chinese imports initiated since 2007. The numerous flaws with this analysis are briefly outlined below:

Public body. DOC found that state-owned banks in China constitute public bodies not because they possess any governmental authority, as the Appellate Body standard requires, but merely because they are owned and controlled by the government. As noted above, the more appropriate analysis in such circumstances would be one that examined whether state-owned banks were entrusted or directed by the Chinese government to provide loans (or loans at discounted rates) to certain industries—an analysis that would likely have produced an affirmative determination—but the DOC could not be bothered to take this additional step.

Benefit/Benchmark. In most investigations, there has been no record evidence of exporters receiving loans at "preferential rates" because the People's Bank of China (PBOC) strictly regulated lending rates during the periods examined. In short, it was impossible for investigated exporters to benefit from loan discounts compared with other, nonpreferred Chinese companies because everyone in China received the same lending rate. To bypass this inconvenient fact, DOC determined that domestic lending rates were distorted because of the predominant presence of the Chinese government in the domestic lending market, and thus utilized an external benchmark to determine benefit. In particular, the agency created a benchmark from a basket of lending rates from supposedly comparable (based on per capita GNI) countries such as Djibouti, Tonga, Lesotho, Namibia, Swaziland, the Republic of Congo, Nigeria, Vanuatu, Cape Verde, Guyana, Micronesia, Suriname, Cameroon, and Angola. Because that basket rate was inevitably higher than the PBOC rate, the resulting comparison created a benefit where none may have existed.

Specificity. The primary evidence of specificity in these cases are vague, high-level policy statements from government officials related to supporting the industry at issue with credit or loans. Even assuming this establishes a specific financial contribution, the benefit received is not specific because, as noted above, lending rates in China are highly regulated, and investigated companies in China receive approximately the same lending rate as comparable domestic companies. DOC was only thus able to establish specificity by using the single element specificity analysis described above.

A closer review of this analysis in the policy lending context reveals disturbing implications. DOC has found a specific financial contribution in the form of government-mandated allocation of loans, through Chinese banks, to certain enterprises (e.g., tire producers). However, there is no record evidence that Chinese exporters actually received any loans that they would not have received in the absence of the alleged program. Meanwhile, DOC has made a separate benefit finding without reference to the alleged financial contribution or its specificity. The benefit calculation is not based on the benefit that would be bestowed by the alleged financial contribution—a misallocation of lending to the exporters in question—but rather the benefit that would be bestowed by a simple preferential lending rate. Yet all enterprises in China received the essentially same preferential lending rate. DOC's disconnected specificity determination directly facilitates this erroneous finding.

Attribution. In many cases, countervailable loan subsidies received by cross-owned affiliates are attributed to the subject exporter regardless of whether the affiliates actually do business with the exporter or have any knowledge of the subsidy program at issue. As a result, subject exporters are said to have received subsidies from these input providers, and their CVD rates increase. For example, in the 2007 investigation *Coated Free Sheet Paper from China*, DOC countervailed policy loans to an affiliated upstream pulp producer and attributed them to the downstream paper exporter, even though the verified factual record demonstrated that the pulp at issue was not and, pursuant to corporate policy, could not be used to make the subject merchandise that was exported to the United States. Although DOC acknowledged that the pulp at issue was not used to make any subject merchandise, it nevertheless attributed the loan subsidies to the downstream exporter because the pulp could theoretically be used to produce the subject merchandise.[116] DOC also attributed to the subject exporter loans to five upstream forestry companies, further increasing the final duty rate for that company.

"Zeroing." In instances where exporters have received numerous loans from state-owned banks, DOC has adopted a policy whereby it will "zero" any instances in which the interest actually paid is more than the interest that would have been due based on the benchmark lending rate. DOC posits that such zeroing is appropriate because "it would be inconsistent with the statute to allow a 'credit' from transactions that did not provide a subsidy benefit and that doing so would be inconsistent with the department's prior practice."[117] Because of such zeroing, the benefit calculated (and thus the subsidy rate for the lending program) is greater than the actual benefit/subsidy received by the exporter.

CVD/NME. The NME antidumping methodology should offset any benefits conferred on domestic exporters and upstream affiliates via loan subsidies. Thus, double counting (and a higher duty for U.S. importers) exists to the extent that the antidumping rate is not reduced by the amount of the loan subsidies found to exist. DOC's new double counting methodology does not account for loan subsidies.

In sum, DOC has initiated an investigation of a subsidy program where no evidence of such a program exists on the record. It has found that state-owned banks are public bodies where no evidence exists of their possession or exercise of governmental authority, and has refused to conduct the proper "entrustment or direction" analysis. It has found a financial contribution in the form of a misallocation of credit rather than actual discounted lending rates, yet calculated a benefit based on the latter situation. Using a constructed interest-rate benchmark disconnected from the Chinese lending market, DOC has determined that loan recipients indeed received a benefit from these discounted loans, and that such subsidies are specific to those exporters, even though everyone in the country received essentially the same lending rate from the same lenders. And, in calculating the total amount of loan subsidies received by a targeted exporter, DOC has ignored any instances in which the recipient paid a loan premium but has added similar loan subsidies received by loosely affiliated input producers.

The result of this process is a punitive duty rate—eventually paid by U.S. importers and consumers—that has no relation to the alleged loan-subsidy program or the real amount of loan subsidies (if any) received by the Chinese exporter. This outcome simply cannot be what is intended by an anti-subsidy law designed to remedy the actual harms caused by actual trade-distorting subsidies.

Notes

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13. 19 USC § 1677(5)(B)-(D).

14. Appellate Body Report, U.S.—"Antidumping and Countervailing Duties" (China), para. 317. U.S. law uses the term "public entity." 19 USC § 1677(5)(B).

15. The WTO Appellate Body described this comparison as follows:

> We also believe that the word "benefit" . . . implies some kind of comparison. This must be so, for there can be no "benefit" to the recipient unless the "financial contribution" makes the recipient "better off" than it would otherwise have been, absent that contribution. In our view, the marketplace provides an appropriate basis for comparison in determining whether a "benefit" has been "conferred," because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favorable than those available to the recipient in the market.

Appellate Body Report, "Canada-Measures Affecting the Export of Civilian Aircraft," para. 157, WT/DS70/AB/R (August 2, 1999), http://docsonline.wto.org/DDFDocuments/t/WT/DS/70ABR.DOC.

16. These guidelines are codified in U.S. law (19 USC § 1677(5)(E)), and DOC's regulations (19 CFR §§ 351.503—351.520) contain detailed instructions for the calculation methodology to be employed with respect to various financial contributions.

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19. The "objective criteria or conditions" mean "criteria or conditions which are neutral, which do not favour certain enterprises over others, and which are economic in nature and horizontal in application, such as number of employees or size of enterprise." The criteria or conditions must be "clearly spelled out in law, regulation, or other official document, so as to be capable of verification."

20. In assessing de facto specificity, WTO Members must account for the extent of diversification of economic activities within the jurisdiction of the granting authority and the length of time during which the subsidy program has been in operation. If a developing country's economy centers around one industry, or if a program has only been in effect for short period of time, then the evidence noted above might not be dispositive of de facto specificity.

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109. 19 CFR § 351.202(i).

110. Note: 19 USC § 1671a(b)(4)(B) prohibits DOC from accepting any "unsolicited" oral or written communications from parties other than domestic companies, unions, or associations who produce the product under investigation.

111. 19 USC § 1671a(B).

112. 19 CFR § 351.505 for loans and § 351.511 for goods/services.

113. 19 CFR § 351.525.

114. 19 CFR § 351.523.

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