SOE Reform

- From experience of developed countries to advice for China

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Table of Contents

List of Abbreviations

BSC	British Steel Corporation
DOC	The U.S. Department of Commerce
ECGD	Export Credits Guarantee Department
EDC	Export Development Corporation
FTA	Free Trade Agreement(s)
FR	Federal Register
GATT	General Agreement on Tariffs and Trade
ITA	The International Trade Administration,
ITC	The U.S. International Trade Commission
MTA	Metropolitan Transportation Authority
NLF	National Loans Fund
OECD	Organisation for Economic Co-operation and Development
RPSP	Risk and Profit Sharing Program
SCM	Subsidies and Countervailing Measures
SOE	State Owned Enterprises
TPP	Trans-Pacific Partnership
USMCA	United States–Mexico–Canada Agreement
USTR	United States Trade Representative
TPP	Trans-Pacific Partnership
CPTPP	Comprehensive and Progressive Agreement for Trans-Pacific Partnership
WTO	World Trade Organization

Executive summary

State-owned enterprises (SOEs) have always been a common form of state intervention in history. State intervention in economy could lead to discontentment by other countries because SOEs could grant or be granted to competitive advantages in the international market. These advantages can take the form of direct subsidies, concessionary financing, state-backed guarantees, preferential regulatory treatment, exemptions from antitrust enforcement or bankruptcy rules, and others.[1] In this paper, the discussion of SOEs' problems revolves around subsidies during the pre-WTO period. Nowadays China's SOEs have drawn much attention in international trade governance and posed challenges to international economic law, so there is an inevitable question in front of China: whether it is time for China's SOEs to reform? This paper aims to sum up some past experience of developed countries. The experience can be used as reference to China's SOEs.

In this paper, we seek to answer the following questions:

- First, have SOEs in other countries led to trade tension with their trading partners?
- Second, if they haven't, then what was the rationale behind, or possible explanation of, the harmonization?
- Third, if they have, then how did they impact trade?
- Fourth, further to question 3, under the circumstances where SOEs have resulted in trade tension, how did those countries eliminate, or at least, diminish the tension?
- Fifth, what experience can be drawn from the four cases concerning China's SOEs?
- Sixth, what advices could this paper give to China's SOEs helping them relieve or eliminate tension in the future?

To answer the first question, a comprehensive analysis of SOEs in the different period, different industries and even specific cases is required. Considering the key purpose of our research, which is, providing historical experience to China's SOE, this paper focuses on the pre-WTO period and analyzes SOEs problems by conducting case studies. However, based on the case studies, the answer to this question is contingent on specific circumstances.

To shed light on the subsequent four questions, this paper uses four cases to analyze the

[1]Kowalski, P. et al. (2013), "State-Owned Enterprises: Trade Effects and Policy Implications", OECD Trade Policy Papers, No. 147, at 4, OECD Publishing, Paris.

role of SOEs in specific situations and find out why SOEs led to tension or not. These four cases are mainly about subsidies through which SOEs grant or be granted advantages causing cross-border effect and raising tension among countries. This paper sums up the solutions that SOEs in four cases took to avoid tension and summarizes some experience for China's SOEs.

To shed light on the last question, this paper reviews existing rules from WTO to FTAs on SOEs' problems trying to show the challenges China's SOEs are facing. Plus, this paper seeks to find solutions to problems of China's SOEs from the competitive neutrality principle.

1 Introduction

State-owned enterprises (SOEs) have long been used as a way of government intervention in economic development. To achieve better economic and social results, SOEs may be used to solve employment problems, to cure market failure, to properly allocate resources, etc. Admitting the benefits SOEs may bring to economy and society, however, SOEs are also accused of disturbing fair competition in market. Specifically, under international trade regime, two issues involve SOEs into debate now and then. The first issue focuses on special privileges SOEs may receive provided by the government, while the second issue focuses on the intermediary status of SOEs as a giver of subsidies from the government. China once used SOEs to operate its planned economy and SOEs proliferated in China. Although the planned economy is at present abandoned by China, the large amount of SOEs still exist and raise some concerns in international trade, such as DS379[2], DS413[3]. Many literatures have discussed the concerns with China's SOEs, but few discussed SOEs in developed countries. We initiate this research to figure out whether like concerns with SOEs were raised indeveloped countries in history.

To find the answer, we looked into cases and literatures about SOEs during the period of 1947 - mid-1990s, when GATT 1947 was in effect and the waves of privatization had not yet started across the world[4] and large amount of SOEs still existed in researched countries. By looking into the *Import Injury Investigations Case Statistics* released by U.S.'s International Trade Comission, we found that the number of countervailing duty cases field in FY 1982 was 113 in total and most of them were about steel industry. In contrast, the number of countervailing duty cases field in one year from FY 1980 to FY 2008 was 44 at most, except for FY 1982. Additionally, we further discovered that in those years, most journals were talking about subsidies.[5] One economic background of that period is a severe slump in the U.S. steel industry as a result of years of neglect, a recession, and an influx of imports by foreign competitors.[6] The other statutory background is that the Trade Agreements Act of 1979 amended the Tariff Act of 1930 in order to implement into U.S. law the international agreements

[2] DS379: United States — Definitive Anti-Dumping and Countervailing Duties on Certain Products from China. https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds379_e.htm

[3] DS413: China — Certain Measures Affecting Electronic Payment Services. https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds413_e.htm

[4] State-owned enterprises — trade effects and policy implications. OECD Trade Policy Papers No. 147. P53.

[5] United States International Trade Comission, IMPORT INJURY INVESTIGATIONS CASE STATISTICS (FY 1980-2008), February 2010.

[6] U.S. INT'L TRADE COMM'N, PUB. No. 1221, CERTAIN STEEL PRODUCTS FROM BELGIUM, BRAZIL, FRANCE, ITALY, LUXEMBOURG, THE NETHERLANDS, ROMANIA, THE UNITED KINGDOM, AND WEST GERMANY 111 (1982) (preliminary determination). Steel industry statistics indicate that the impact of the unfairly traded imports is one factor contributing to the overall poor economic health of the U.S. steel industry. See *Id* at 114-115. Other factors causing harm to the steel industry include the relatively depressed U.S. economic conditions, high interest rates and labor costs, and increased foreign competition in an industry characterized by an inelastic demand. *Id* at 114-119.

negotiated and signed by the United States at the Tokyo Round Multilateral Trade Negotiations, by enacting new antidumping and countervailing duty laws.[7] Judging from the above, it was obvious that subsidy, a method of state intervention, was one reason causing trade tension among countries around 1982. More importantly, SOEs played an important role in conveying subsidy. Thus, this paper selected four cases where the subsidy granted to SOEs or was granted by SOEs during the period from 1978 to 1985.

Each case shows how one enterprise was determined as an SOE and what was the concern for such SOE. For each case, the solution to the trade tension raised by SOE will be elaborated. At the end of the case studies, a conclusion about the experiences from the case studies will be given. Further, we will discuss SOE-related matters in present days, and give advice for Chinese government and SOEs on how to avoid trade tensions.

In this research, we take the first step to analyze SOE-related concerns in developed countries. This theoretical analysis could build a comprehensive framework for study of SOEs, and the case studies canshow how SOEs were operated, whether trade tensions were raised, and how the tension was eased. Theoretically, this research could give some hints on analyzing legitimacy of SOEs' actions based on the discussed cases. Practically, it can act as a reference for Chinese government and SOEs before they take certain policies and actions.

The present research consists of four parts. Part 1 is the introduction of this paper which shows why and how we will do this research. Part 2 discusses the definition of SOEs. Part 3 are case studies which can help us learn from the past. Part 4 presents advice for Chinese government and SOEs on how to avoid being accused of disturbing fair market competition.

[7] Jonathan T. Suder, *Cumulation of Imports in Antidumping and Countervailing Duty Investigations,* 17 Geo. Wash. J. Int'l L. & Econ. 463 (1983)

2 What is SOE

In this part, we first look at the overall relationship between the state and enterprises. We also present the existing definitions of SOEs to see how they work under each context. We then propose a definition for the purpose of this article.

2.1 Introduction

2.1.1 Enterprises are the key of a country's economy, In order to achieve specific economic goals, such as economy growth and industry development, a state often influence the direction of enterprises by various means. A state may formulate relevant laws to regulate the behavior of enterprises, which has an impact on the cost and profits of enterprises to achieve the purpose of stimulation or restriction. For example, tax law, environmental law and labor protection law all play a significant role in industry policy, which may be considered as a form of state intervention. In respect to the macro economic policy, the control of interest rate, money supply and the targeted credit expansion or restriction for certain companies are all the methods employed to support or restrict the development of targeted businesses.

On a micro level, the government could participate in an industry by establishing huge state-owned enterprises in this industry and implementing the above mentioned policies. Because some SOEs bear important public functions or are key to the development of the country's specific industry, the state will support SOEs' development by investment, tax incentives, subsidies, etc. In the international trade, the preferential treatment to state-owned enterprises is easy to be ascertained as subsidies, which would raise trade disputes such as countervailing investigations. This is also the main reason why this paper explore SOEs and the controversy they result in.

2.1.2 According to the trade policy paper published by OECD[8], forms of state ownership can be various and the state can hold various levels of equity of enterprises.[9] In order to consistently assess the role and trade effects of SOEs in global trade, the policy paper adopts a definition of SOEs as "*a majority state-owned enterprise*", though it also discusses other forms of state ownership. As for what 'majority' means, this paper quotes the

[8] See OECD Trade Policy Paper No.147, *State-Owned Enterprises – Trade Effects and Policy Implications,* page 10

[9] The government can either hold all shares, or have a majority or minority stake. Even when a government has a minority share in an enterprise, it can still be a controlling share, when a government is still the biggest owner or has a golden share, which allows de facto control regardless of formal voting rights.

classification given by Orbis databases – that is, "a firm is classified as an SOE when a state, a government or a public authority is the ultimate owner of that firm and holds more than 50.01% of the firm's shares." Firms with lower percentage of shares by the state are considered private[10]. Here the mere standard of ascertaining an SOE is the share owned by the state of the enterprise.

2.2 Possible definitions of SOEs

Generally, the term "state-owned enterprise" provides only an approximate description of the complexity of forms and organizations that state companies may assume.[11] The standards of state-owned enterprises may be very different in different countries and different legal texts, while the definitions in WTO covered agreements and free trade agreements ("FTA") can still be referred to for hints. For the FTAs specially, it is the purpose of the FTA that determines the definitions of each term, the definition of SOE included. Considering there is no uniform definition of the SOEs for the time being, various possible illustrations are given below for reference.

2.2.1 SOEs in US-led FTAs

The United States has engaged in many FTAs with its trading partners, some of which have SOEs defined and stipulated in the provisions. More often than not, it is the purpose of the FTA that drives the definition of SOEs. For instance, in US-SG Letter Exchange on SOE Transparency[12] which constitutes part of the Trans-Pacific Partnership (TPP) full text, the US Ambassador specifically confirms that Singapore shall comply with the obligations set out in Article 17.10.1 (Transparency)[13] of the TPP Agreement[14]. The transparency requirement in Article 17 is employed under the definition of SOE, while it is derived from the overall transparency requirement of the TPP Agreement as a whole. As indicated in the preamble, as a whole, the TPP Agreement is to "promote transparency governance and the rule of law, and eliminate bribery and corruption in trade and investment"[15], which implicitly considers

[10] See OECD Trade Policy Paper No.147, *State-Owned Enterprises – Trade Effects and Policy Implications,* page 20

[11] See Pier Angela Toninelli, *The Rise and Fall of State-Owned Enterprise in the Western World* (first published in 2000, digitally printed version 2008), page 4-5

[12] See the letter under the section of Related Instruments under TPP Final Table of Contents at https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text, last visited at Dec 24, 2018

[13] See *Trans-Pacific Partnership*, page 14, Article 17.10 under the sub-title Transparency

[14] See the second paragraph of the US-SG Letter Exchange on SOE Transparency

[15] See the Preamble of *Trans-Pacific Partnership*, paragraph started with PROMOTE, at https://ustr.gov/sites/default/files/TPP-Final-Text-Preamble.pdf, last visited on Dec 24, 2018

transparency as one of the goals the TPP wants to achieve.

The TPP Agreement, is a most well-known FTA the United States had entered into previously. It is a trade agreement between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam, and the United States signed on 4 February 2016.

Under the scope of TPP,[16] state-owned enterprise means *an enterprise that is principally engaged in commercial activities in which a Party:*

(a) directly owns more than 50 per cent of the share capital;

(b) controls, through ownership interests, the exercise of more than 50 per cent of the voting rights; or

(c) holds the power to appoint a majority of members of the board of directors or any other equivalent management body.

After the Office of the U.S. Trade Representative (USTR) issued a letter to signatories of the Trans-Pacific Partnership Agreement, the United States has formally withdrawn from the agreement per guidance from the President of the United States.[17]

Though defunct as a whole now, the provisions of TPP still remain valuable for the purpose of refence. For one thing, most of its provisions are incorporated into the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)[18], a trade agreement between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam – the remaining members of the former TPP except the United States. Article 1 of CPTPP states,[19] with regard to the adoption of TPP provisions, that ".. the provisions of the Trans-Pacific Partnership Agreement, done at Auckland on 4 February 2016 ("the TPP") are incorporated, by reference, into and made part of this Agreement mutatis mutandis, except for Article 30.4..". For another, the United States–Mexico–Canada Agreement ("USMCA") developed the concept and identification of SOEs based on the TPP provision, making the TPP version noteworthy[20]. As for the development in and

[16] See *Trans-Pacific Partnership*, page 4, Article 17.1
[17] See this introduction on USTR's official website at https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership, last visited on Dec 18, 2018
[18] The full text of the CPTPP can be found on, for instance, Canada government's official website at https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/index.aspx?lang=eng, last visited on Dec 18, 2018
[19] See *Comprehensive and Progressive Agreement for Trans-Pacific Partnership,* Article 1, section 1
[20] As shall be mentioned below, Chapter 22 of USMCA is inherited from Chapter 17 of TPP Agreements

comparison with USMCA, we will get back to this in Section 4.1.2.

2.2.2 SOEs in WTO covered agreements

WTO itself has no direct stipulation of what state owned enterprise means in its covered agreements. However, there are many hints for reference when it mentions relevant concepts. Among all this related provisions, General Agreement on Tariffs and Trade ("GATT" or "GATT 1994") and the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") should be the most notable two. For definition of the term "subsidy" in the SCM Agreement, it contains three basic elements: (i) a financial contribution (ii) by a government or any public body within the territory of a Member (iii) which confers a benefit.[21] All three of these elements must be satisfied in order for a subsidy to exist. As for how to ascertain a "public body" and its implications, we will discuss it in the last part of this paper.

GATT 1994 itself didn't use the exact term "state owned enterprise" to name the type of companies mentioned in this paper, while Article XVII[22] writes under the sub-title State Trading Enterprises, "Each contracting party undertakes that if it establishes or maintains a State enterprise, wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges, such enterprise shall, in its purchases or sales involving either imports or exports, act in ...".

As can be concluded from this provision, a "State Trading Enterprise" is *an enterprise which is established or maintained by a state or which has been given exclusive or special privileges, especially in its purchases or sales involving either imports or exports.*

However, the definition here is not specified. Later in < Understanding on the interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994>,[23] Para 1 introduces the "working definition" of State Trading Enterprise: "*Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through*

[21] See this introduction part "Coverage of the Agreement" on WTO official website at https://www.wto.org/english/tratop_e/scm_e/subs_e.htm, last visited on Dec 18, 2018 or in *Agreement on Subsidies and Countervailing Measures*, Article 1.1, Section (a)(1).
[22] See Article XVII of <The General Agreement on Tariffs and Trade> (GATT 1947)
[23] See the detailed description of activities of the state trading enterprises in <Understanding on the interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994>

their purchases or sales the level or direction of imports or exports".

The "working definition" is explicitly stated to be without prejudice to the substantive provisions of Article XVII, while the working definition does not explain the meaning of "exclusive or special rights".[24]

2.2.3 SOEs in EU proposal

The *EU proposal on State-owned enterprises, enterprises granted special rights or privileges, and designated monopolies*, which constitutes legal text for state-owned enterprise and other enterprises in the EU-Indonesia FTA, defines "state-owned enterprise" as[25] *an enterprise, including any subsidiary, in which a Party[26], directly or indirectly:*

(i) owns more than 50% of the enterprise's subscribed capital or the votes attached to the shares issued by the enterprise;

(ii) can appoint more than half of the members of the enterprise's board of directors or an equivalent body; or

(iii) exercises or has the possibility to exercise control over the enterprise.

As can be seen in the definition mentioned above, the state can not only own a majority of capital or the votes, but also have the appointment rights of a majority of board members or have "control" over the enterprise, if the enterprise is to be identified as an SOE.

2.3 The definition of SOEs for the purpose of this paper

The way of defining SOEs can vary from one document to another, serving different contexts and specific goals. For the purpose of this paper, we think it will be safe to employ a more traditional and conservative definition of state owned enterprise here. Regarding the extensive definition of SOEs, for instance, in United States–Mexico–Canada Agreement[27], we will not take it as the exact definition of in the main body of this paper, while we will get back to it when discussing the possible impacts of it on Chinese SOEs. We hereby define a state-owned enterprise as[28] *an enterprise in which a state, directly or indirectly, owns more than 50% of the enterprise's shares, or holds*

[24] See *WTO and SOEs: Overview of Article XVII and related provisions of the GATT 1994* (European University Institute working paper RSCAS 2017/08). page 4.
[25] See *EU proposal on State-owned enterprises, enterprises granted special rights or privileges, and designated monopolies*, Article X.1, Section (a).
[26] The word "Party" here refers to any of the signing party of this proposal.
[27] See Section 4.1.2 of this paper.
[28] This definition is without prejudice to any definition mentioned below in real cases and other discussion.

the power to appoint a majority of members of the board of directors.

3 Case studies: learning from the past

3.1 Introduction to this part

In this part, we will introduce four cases. The first one is the case where the SOE didn't lead to trade tension. In the last three cases, the SOEs had resulted in much trade tension. The three cases involving subsidies show two ways of subsidization: where subsidies were provided by the state to the SOE in the first case, and where subsidies were provided by SOEs to other enterprises in the other two cases. The investigations related to the last three cases were initiated after 1979, when the U.S. countervailing law was essentially changed to conform with the agreement reached in the Tokyo Round of Multilateral Trade Negotiations. The Trade Agreement Act of 1979 requires an "injury test" in all investigations, which remain unchanged till now. Therefore, the lessons learned from the last three cases may still be enlightening.

The first case is about an SOE that the government has provided guarantees on the firm's loans, and there have been increases in the government's capitalization of this SOE.

In the second case, the DOC determined that four programs constitute subsidies given to the SOE, *i.e.* BSC.

The third case is about that the export credits provided by government owned banks constitutes subsidy.

The fourth case involves two electricity supply contracts. The first contract was determined by the DOC to provide subsidies by an SOE with preferential electricity rates discount. The second contract is determined to be the result of amendment of the first contract after the determination of subsidies, and the second one was determined not to confer subsidies.

3.2 Case study: Papermaking machines and parts thereof from Finland

The case occurred in 1978, when many Finnish papermaking machine companies were accused of subsidies by US domestic petitioners, and Valmet was one of them. The alleged reason is that government investment and loan guarantees from government are considered to constitute subsidies. In the course of studying the case, we found that the US government determined that the government manners did not constitute subsidy, and the reasoning process was an important reference for China's state-owned enterprises. From this case, we can conclude that the government's shareholding itself is not subsidy, but the commercial and competitive benefit. The analysis of US is consistent with the idea of competition neutrality, equal status of private

and state-owned enterprises, which means SOEs should not have any competitive advantages due to government. The realization of this concept can help state-owned enterprises avoid being accused of accepting subsidies. This case is one of the few cases where SOEs have not caused trade tension, and competition neutrality is a good reference for China. That is the main reason for choosing this typical case.

3.2.1 Case background

Valmet is a commercial enterprise, a state-owned company, the Finnish government contributes capital to and owns the shares of Valmet Oy.

The SOE is a Finnish manufacturer of paper machinery and parts. In the past several years, the Finnish government has increased the capitalization of Valmet, and some of the investment has been directly distributed to the papermaking machinery business.

Valmet was one of the exporters of the product to the United States. On February 9, 1978, the US Customs Service, Treasury Department, received a petition, insisting that the payment or grant from Finnish government for Valmet Oy constitutes payment or bestowal of a bounty or grant referred to in section 303 of the Tariff Act of 1930, as amended (19 U.S.C. 1303). Section 303 is about the provisions of countervailing duties.

"Whenever any country, dependency, colony, province, or other political subdivision of government, person, partnership, association, cartel, or corporation shall pay or bestow, directly or indirectly, any *bounty or grant* upon the manufacture or production or export of any article or merchandise manufactured or produced in such country, dependency, colony, province, or other political subdivision of government, and such article or merchandise is dutiable under the provisions of this Act, then upon the importation of any such article or merchandise into the United States, whether the same shall be imported directly from the country of production or otherwise, and whether such article or merchandise is imported in the same condition as when exported from the country of production or has been changed in condition by remanufacture or otherwise, there shall be levied and paid, in all such cases, in addition to the duties otherwise imposed by this Act, an additional duty equal to the net amount of such *bounty or grant*, however the same be paid or bestowed. The Secretary of the Treasury shall from time to time ascertain, determine or estimate, the net amount of each such bounty or

grant, and shall declare the net amount so determined or estimated".[29]

The petition declares some conducts made by the Finnish government, including: "the Finnish government's capitalization of Valmet, which also guarantees the company's domestic and international loans under conditions not available to other companies."[30] The US Customs services has initiated an investigation on the basis of information available April 14, 1978.

But in the preliminary stage, the Custom Service did not find any evidence that Finnish government's shareholding in Valmet has made Valmet more commercially advantageous than private paper machine manufacturers. In the perspective of U.S. Treasury department, "The mere fact that the government provides capital for and owns shares of commercial enterprises is not inherently countervailable."[31] Therefore, it is determined that the Finnish government's ownership of the company and the government's investment in the company could not be considered as a "bounty or grant" on this company.

Since the preliminary determination, addition to the ownership of the Finnish government, any other possible factors for the favorable treatment or subsidies of the Valmet paper machinery business have been reviewed. It has been found that when loans are guaranteed by the Finnish government, Valmet has received benefits from preferential interest rates from commercial bank. But it is also determined that the benefits was only "0.02 percent"[32], which is a negligible amount.

Based on the above information, the Finnish government has exactly provide some benefits for Valmet, but these benefits are "de minimis."[33] Valmet is not more favorable due to the ownership of government than any other private enterprises in papermaking machine industry. Finally, it is determined no bounty or grant is being paid or bestowed directly or indirectly, within the meaning of section 303 of the tariff act of 1930 (as amended) (19 U.S.C 1303).

3.2.2 The reason why SOE did not lead to trade tension in this case

It is worth noting that the US Customs Service analyse the status of the

[29] Section 303 of the tariff act of 1930.
[30] Federal Register Vol.43, No.73, April 14, 1978. page 15825. (This citation could be short for "43 Fed. Reg. 15825", hereafter citations from Federal Register will be adopted as the simplified one.)
[31] 43 Fed. Reg. 38657.
[32] 44 Fed. Reg. 10451.
[33] 44 Fed. Reg. 10451.

company in papermaking industry, Whether it is from government holdings or government-guaranteed loans, the US believes that the company has not obtained a commercial advantage over private companies, which is the most important reason for not constituting bounty or grant. This analysis approach is consistent with the nature of competitive neutrality, although the concept of competitive neutrality does not appear at this time.

According to an OECD report, "Competitive neutrality occurs where no entity operating in an economic market is subject to undue competitive advantages or disadvantages."[34]

State-owned enterprises should not have a comparative advantage than the private, which is the outcome advocated by competition neutrality idea. Finnish government achieves the goal of competitive neutrality at least among Valmet Oy and other private enterprises in the papermaking machinery industry, which is proved by the investigation outcome and relevant analysis made by the US Treasury Department.

Because of the basically equal status of SOE and private enterprises, the ownership and increased capitalization of Finnish government could not be considered as "bounty or grant". If it is considered that it does not constitute subsidies because of competition neutrality, it means the realization of competition neutrality in a industry can help avoid international trade disputes arising from the corresponding SOEs. Therefore, Establishing a competitive neutral macro environment between the SOEs and the private is a practical way that can protect state-owned enterprises from countervailing duties.

3.3 Case study: British Steel Corporation

"Since the late 1970s, U.S. steelmakers have stressed the need for general protectionist measures to stave off low-priced imports, which they argue are unfairly subsidized and produced by exploited, low-wage laborers. The steel industry has also suggested that the U.S. needs direct government action to offset the effect of foreign subsidies, since artificial exchange rates, tax rebates, and below-cost prices have provided foreign products with a margin of advantage they would not be able to derive from production cost advantages alone." [35] Between 1970s-1980s, a large number of

[34] Competitive neutrality: Maintaining a level playing field between public and private business. OECD 2012. page17.
[35] Brian L. Zimbler, Subsidies Law and Adjustment Policies: The 1982 EEC-US Steel Dispute Revisited, 8 Fletcher F. 397 (1984) at 409.

investigations[36] involving steel were initiated. The British Steel Corporation (hereinafter: BSC) case is part of the general protectionist measures.

3.3.1 The factual background of the BSC case

On October 7, 1982, members of the Tool and Stainless Steel Industry of the United States[37] and the United Steelworkers of America filed a petition with the U.S. Department of Commerce (hereinafter: DOC) and the U.S. International Trade Commission (hereinafter: ITC) alleging that producers, manufacturers, or exporters in the United Kingdom of stainless steel sheet, strip, and plate receive subsidies within the meaning of section 771(5) of the Tariff Act of 1930, as amended (19 U.S.C 1677(5))[38] (hereinafter: the Act) and that an industry in the United States is being materially injured and threatened with material injury by reason of allegedly subsidized imports of stainless steel sheet, strip and plate from the United Kingdom.

Accordingly, on October 7, 1982, the ITC instituted preliminary countervailing duty investigations (Nos. 701-TA-195 and 196) under section 703(a) of the Act[39]. Notice of the institution of preliminary countervailing duty investigations was published in the Federal Register on October 20, 1982 (47 Fed. Reg. 46781). Meanwhile, on November 2, 1982, the International Trade Administration, U.S. Department of Commerce (hereinafter: ITA) issued initiation of countervailing duty investigations (47 Fed. Reg. 49692) under section 702(c) of the Act[40].

On November 22, 1982, the ITC published Determinations of the Commission in Investigations Nos. 701-TA-195 and 196 (Preliminary)[41]. Notice of the preliminary injury determinations was published in the Federal Register on December 1, 1982 (47 Fed. Reg. 54180).

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[36] The investigations include, but not limited to:
Stainless Steel and Alloy Tool Steel: Report to the President on Investigation No. TA-201-5 …, USITC Publication 756, January 1976.
Stainless Steel and Alloy Tool Steel: Report to the President on Investigation No. TA-203-3 …, USITC Publication 838, October 1977.
Stainless Steel and Alloy Tool Steel: Report to the President on Investigation No. TA-203-5 …, USITC Publication 968, April 1979.
Stainless Steel Sheet and Strip from West Germany: Determination of the Commission in Investigation No. 731-TA-92 (Preliminary)…, USITC Publication 1252, June 1982.
Stainless Steel Sheet and Strip from France: Determination of the Commission in Investigation No. 731-TA-95 (Preliminary)…, USITC Publication 1264, June 1982.
Stainless Clad Steel Plate from Japan: Determination of the Commission in Investigation No. 731-TA-50 (Final)…, USITC Publication 1270, July 1982.
Stainless Steel and Alloy Tool Steel: Report to the President on Investigation No. TA-201-48…, USITC Publication 1377, 1983.

[37] Allegheny Ludlum Steel Corporation; Armco Inc.; Carpenter Technology Corporation; Colt Industries, Inc. of the Crucible Materials Group; Eastern Stainless Steel Company; Electralloy Corporation; Guterl Special Steel Corporation; Jessop Steel Company; Jones & Laughlin Steel Incorporated; Republic Steel Corporation. Universal Cyclops Speciality Steel Division of the Cyclops Corporation; Washington Steel Corporation, 47 Fed. Reg. 49692.

[38] 19 U.S.C. § 1677(5) (1979).

[39] 19 U.S.C. § 1671(b) (1979).

[40] 19 U.S.C. § 1671(a) (1979).

[41] STAINLESS STEEL SHEET AND STRIP AND STAINLESS STEEL PLATE FROM THE UNITED KINGDOM, Determinations of the Commission in Investigations Nos. 701-TA-195 and 196 (Preliminary) USITC Publication 1319, November. 1982.

Then on December 17, 1982, the ITA published the notice of postponement of countervailing duty preliminary determinations pursuant to section 703(c)(2) of the Act[42]. In accordance with section 703(c)(1) of the Act[43], the ITA determined that these cases are extraordinarily complicated and the ITA intended to issue countervailing duty preliminary determinations not later than February 4, 1983.[44]

On February 10, 1983, the ITA issued preliminary affirmative countervailing duty determinations in the Federal Register (48 Fed. Reg. 6146). The ITA determined that BSC was established by an Act of Parliament on March 22, 1967, under the provisions of the Iron and Steel Act of 1967. The 1967 Act combined 14 steel companies[45], creating the nationalized British Steel Corporation.[46] The ITA also found that BSC is the only known producer and/or exporter in the United Kingdom of stainless steel sheet and plate exported to the United States.[47] This countervailing duty investigation is mainly initiated against BSC.[48] Then the ITA determined that the following four programs are preliminarily found to confer subsidies: public dividend capital and new capital, national loans fund loans and loan conversions, regional development grants, and iron and steel industry training board grants.[49] It is noted that the program, transportation assistance, is preliminary determined not to confer subsidies. The ITA found that BSC appears to contact with British Rail[50] on an arm's length basis and to pay commercial rates on stainless steel shipments. Since no preferential treatment accorded to BSC on shipments by rail was found, the ITA preliminary determined that the rail freight charges on stainless steel shipments are not preferential and do not result in the payment or bestowal of a subsidy.[51] During verification the ITA finally found in its final determination that BSC didn't use British Rail for shipments of

42 19 U.S.C. § 1671(b) (1979).
43 See *supra* note 39.
44 47 Fed. Reg. 56527.
45 The 14 companies nationalized and named in Schedule 1 of the Iron and Steel Act of 1967, They are: (1) Colvilles Limited.; (2) Consett Iron Company Limited.; (3) Dorman, Long & Co., Limited; (4) English Steel Corporation Limited.; (5) G.K.N. Steel Company Limited.; (6) John Summers & Sons Limited.; (7) The Lancashire Steel Corporation Limited.; (8) The Park Gate Iron and Steel Company. Limited.; (9) Richard Thomas & Baldwins Limited.; (10) Round Oak Steel Works Limited.; (11) South Durham Steel and Iron Company Limited.; (12) The Steel Company of Wales Limited.; (13) Stewarts and Lloyds, Limited.; (14) The United Steel Companies Limited.
46 48 Fed. Reg. 19049.
47 48 Fed. Reg. 6147.
48 Arthur Lee and Sons, Ltd., is the only known producer and/or exporter in the United Kingdom of stainless steel strip exported to the United States. However, this company is rarely mentioned in the *Analysis of Programs* in the Federal Register (48 Fed. Reg. 6146). Moreover, an industry in the United States is not materially injured or threatened with material injury, and the establishment of an industry in the United States is not materially retarded, by reason of imports of stainless steel strip from the United Kingdom, see STAINLESS STEEL SHEET AND STRIP FROM THE FEDERAL REPUBLIC OF GERMANY AND FRANCE AND STAINLESS STEEL SHEET AND STRIP AND PLATE FROM THE UNITED KINGDOM, Determinations of the Commission in Investigations Nos. 701-TA-195 and 701-TA-196 (Final) USITC Publication 1391, Jun. 1983.
49 48 Fed. Reg. 6146.
50 The ITA found that the British Rail is the totally government owned rail company in its final affirmative countervailing duty determinations. See 48 Fed. Reg. 19052.
51 48 Fed. Reg. 6149.

finished stainless steel products, but rather for shipments of scrap used as input for stainless steel sheet and plate.[52] The conclusion was the same that no subsidy was being provided to BSC under the program, transportation assistance, based on the same reason that BSC didn't appear to receive preferential rates. What's special in the analysis of the program, transportation assistance, is that both BSC and British Rail are SOEs. But the nature of being SOE does not necessarily mean that the SOE may receive bounties or grants which constitute subsidies or confer subsidies. It is the preferential treatment that resulted in inconsistency with commercial consideration,[53] which is critical in the determination of a countervailing duty investigation.

Later, on February 24, 1983, notice of the institution of final countervailing duty investigations, under section 705(b) of the Act[54] by the ITC, was published in the Federal Register (48 Fed. Reg. 8876).

On April 27, 1983, the ITA published the notice of final affirmative countervailing duty determinations pursuant to section 705(d) of the Act[55] in the Federal Register (48 Fed. Reg. 19048) and determined that certain benefits which constitute subsidies within the meaning of the countervailing duty law are being provided to manufacturers, producers, or exporters in the United Kingdom of stainless steel sheet, strip and plate.[56] Since the final affirmative countervailing duty determinations were instituted by the ITA, the ITC published Determinations of the Commission in Investigations Nos. 701-TA-195 and 701-TA-196 (Final)[57]. In order to make final determinations, the ITC first discussed the question of like product and domestic industry, then examined the condition of the industries, and finally considered whether the necessary causal connection exists between the condition of the domestic industries and the subject imports. The ITC then determined that an industry in the United States is not materially injured or threatened with material injury, and the establishment of an industry in the United States is not materially retarded, by reasons of imports of stainless steel sheet and strip from the United Kingdom and an industry in the United States is materially injured by reason of imports of stainless steel plate from the United Kingdom.[58]

Until then, the countervailing duty investigations terminated.

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52 48 Fed. Reg. 19052.
53 19 U.S.C. § 1677(5)(B)(i) (1979).
54 19 U.S.C. § 1671(d) (1979).
55 See *supra* note 51.
56 48 Fed. Reg. 19048.
57 STAINLESS STEEL SHEET AND STRIP FROM THE FEDERAL REPUBLIC OF GERMANY AND FRANCE AND STAINLESS STEEL SHEET AND STRIP AND PLATE FROM THE UNITED KINGDOM, Determinations of the Commission in Investigations Nos. 701-TA-195 and 701-TA-196 (Final) USITC Publication 1391, Jun. 1983 (hereinafter cited as ITC Investigation (Final)).
58 *ITC Investigation (Final)*, *supra* note 49 at 1.

Section 703(d) of the Act [59] provides that if the preliminary determination of the ITA is affirmative, the ITA shall order the suspension of liquidation of all entries of merchandise subject to the determination which are entered, or withdrawn from warehouse, for consumption on or after the date of publication of the notice of the determination in the Federal Register, and shall order the posting of a cash deposit, bond, or other security, as it deems appropriate, for each entry of the merchandise concerned equal to the estimated amount of the net subsidy. The ITA directed the U.S. Customs Service to suspend the liquidation and to require a cash deposit or bond in the Federal Register (48 Fed. Reg. 6149) in accordance with the section 703 of the Act.

Since the ITA and the ITC have separately determined that the certain benefits which constitute subsidies within the meaning of the countervailing duty law are being provided to BSC in the United Kingdom of stainless steel plate and that these imports are materially injuring a U.S. industry. All unliquidated entries of this merchandise (stainless steel plate) entered, or withdrawn from warehouse, for consumption on or after February 10, 1983, the date of publication of the ITA's preliminary determination, are liable for the possible assessment of countervailing duties. Further, a cash deposit of estimated countervailing duties must be posted on all such entries made on or after publication of the countervailing duty order in the Federal Register in accordance with section 706(b)(1) of the Act[60]. On June 23, 1983, Alan F. Holmer, *Deputy Assistant Secretary for Import Administration*, directed the U.S. Customs Service to assess countervailing duties in accordance with sections 706(a)(1) and 751 of the Act and to require a cash deposit equal to the amount to the estimated net subsidy for all entries of stainless steel plate imported from the United Kingdom. The amount to be deposited was 19.31 percent *ad valorem*.[61]

After the publication of the countervailing duty order on stainless steel plate from the United Kingdom in the Federal Register (48 Fed. Reg. 28690) on June 23, 1983, the petitioners, Allegheny Ludlum Steel Corporation, Armco, Inc., Jessop Steel Company, LTV Specialty Steels, Inc., Cyclops Corporation, Washington Steel Corporation, and the United Steelworkers of America, informed the DOC that they are no longer interested in the order and stated their support of revocation of

[59] 19 U.S.C. § 1671b (1979).
[60] 19 U.S.C. § 1671e (1979). This subsection provide as follow:
(b) IMPOSITION OF DUTIES.—

(1) GENERAL RULE.—If the Commission, in its final determination under section 705(b), finds material injury or threat of material injury which, but for the suspension of liquidation under section 703(d)(1), would have led to a finding of material injury, then entries of the merchandise subject to the countervailing duty order, the liquidation of which has been suspended under section 703(d)(1), shall be subject to the imposition of countervailing duties under section 701(a).
[61] 48 Fed. Reg. 28690.

the order.[62] Section 751(b) of the Act[63] provides that whenever the administering authority or the Commission receives a request for the review, it shall conduct such a review after publishing notice of the review in the Federal Register. Section 751(c) of the Act[64] provides that the administering authority may revoke, in whole or in part, a countervailing duty order after review under this section. As a result of the review, the DOC preliminary determined that the domestic interested parties' affirmative statement of no interest in continuation of the countervailing duty order on stainless steel plate from United Kingdom provides a reasonable basis for revocation of the order. Therefore, the DOC tentatively determined to revoke the order on stainless steel plate from the United Kingdom effective March 1, 1986.[65] On August 14, 1986, the DOC published in the Federal Register (51 Fed. Reg. 29144) the final results of changed circumstances administrative review and revocation of countervailing duty order on stainless steel plate from the United Kingdom (48 Fed. Reg. 28690). The DOC finally determined to revoke the order effective March 1, 1986, and instructed the Customs Service to proceed with liquidation of all unliquidated entries of stainless steel plate exported on or after March 1, 1986 without regard to countervailing duties and to refund any estimated countervailing duties collected with respect to those entries.[66]

3.3.2 The role of SOE in this case

Based on the Iron and Steel Act of 1967, BSC is a SOE in accordance with the definition in this paper.

A full consideration of the Act would be very lengthy. Certain sections of the 1967 Act illustrate the state-owned characteristics of BSC as follow:

Section 1 (The National Steel Corporation) of the 1967 Act provides the establishment of the corporation. This section stipulates that the corporation shall be a public authority, as well as a body corporate. Subsection (3), (4) and (5) provide the appointment of the corporation. The corporation shall consist of a chairman and a minimum of seven and a maximum of twenty members, and the chairman and the other members shall be appointed by the Minister of Power. As soon as possible after the appointment, the Minister shall lay before each House of Parliament a statement of the term for which he has been appointed.

Section 2 (Powers of the Corporation) sets out the powers of the corporation. This section entitles the corporation the power to carry on

62 51 Fed. Reg. 18476
63 19 U.S.C. § 1675(b) (1979).
64 19 U.S.C. § 1675(c) (1979).
65 51 Fed. Reg. 18476.
66 51 Fed. Reg. 29145

any iron and steel activities. The corporation shall have power to carry on any other activities which any publicly-owned company is for the time being authorized by its memorandum of association or, as the case may be, by its charter of incorporation or other charter to carry on or any company which at any time was publicly-owned was at any time so authorized to carry on, with the consent of, or in accordance with the terms of any general authority given by, the Minister.

Section 3 (General duty of the Corporation) says that it shall be incumbent on the corporation to further the public interest.

Section 4 (Duty of the Corporation to review their affairs and report to the Minister) stipulates that the corporation shall undertake a review of their affairs for the purpose of determining whether the carrying on of the activities that have fallen to be carried on under their ultimate control is organized, so far as regards the direction thereof, in the most efficient manner and to report their conclusions to the Minister. And the Minister shall lay before each House of Parliament a copy of each report under this section.

Obviously, BSC was substantially controlled by the government of the United Kingdom through direct influence by the Minister of Power back then.

It is noted that during 1982-1983 in which the countervailing duty investigations were undergoing, an Act to consolidate certain enactments relating to the BSC and the iron and steel industry entered into force on July 13, 1982.[67] However, the state-owned characteristic of BSC has not change by the 1982 Act. Because section 1 (The British Steel Corporation) of the 1982 Act reiterates that the corporation shall continue to be a public authority. A slight difference between this section and section 1 of the 1967 Act is about the appointment. The 1982 Act says that the chairman and the other members of the corporation shall be appointed by the Secretary of State, not the Minister of Power.

Since BSC was a SOE, BSC was qualified for the National Loans Fund (hereinafter: NLF). “The NLF is a depositary of money raised through government borrowings. Lending from the NLF is not generally available, but is limited to nationalized British companies. BSC was expressly authorized to borrow from the NLF’s predecessor fund (the Consolidated Fund) by the Iron and Steel Act of 1967, and from the NLF by the Iron and Steel Act of 1975.”[68] Then the program, the NLF, was found to confer subsidies to BSC by the DOC in its final affirmative determinations (48 Fed. Reg. 19048).

[67] Iron and Steel Act 1982 c. 25
[68] 48 Fed. Reg. 19050.

3.3.3 Solution to the BSC case --- settlement agreement

On May 18, 1983, plaintiffs (British Steel Corporation and British Steel Corporation, Inc.) commenced the instant action (Court Nos. 83-5-00732) contesting the final affirmative countervailing duty determination issued by the ITA, which was published in the Federal Register on April 27, 1983 (48 Fed. Reg. 19048). After the ITA issued its final countervailing duty order and published the notice of the order in the Federal Register on June 23, 1983 (48 Fed. Reg. 28690), plaintiffs commenced a second lawsuit (Court Nos. 83-7-01032) challenging ITA's countervailing duty order of June 23, 1983. Since then, lawsuits pertaining to the countervailing duty investigations between BSC and United States lasted until 1988 (British Steel Corp. v. United States, 12 C.I.T. 558, SLIP OP. 88-76)

On May 25, 1988 the parties[69] reached a settlement agreement and submitted the joint consent motion and agreement to the United States Court of International Trade. The parties mutually agree that British Steel Corporation and British Steel Corporation, Inc. shall make payment of certain sum to the United States in full and final settlement of the alleged liability.

3.4 Case study: Export Development Corporation

Certain Rail Passenger Cars and Parts Thereof From Canada: where subsidies were provided by the SOEs.

In 1978-1984, a number of products imported into the United States have benefitted from subsidized export credits.[70] In practice, these export credits were mostly provided by foreign official agencies to purchasers of goods and, at rates below commercial rate. This kind of practice were always determined to constitute a subsidy and distorted the domestic market. In response, American manufacturers have filed countervailing duty petitions against these subsidized imports with the International Trade Administration (ITA). In this case, the petition led to a precedent-setting decision by the ITA which established that countervailing duties can be imposed against subsidized export credits under U.S. law.[71]

Until now, export credits are still an important way for many countries,

[69] Plaintiffs, British Steel Corporation and British Steel Corporation, Inc.; Defendants, the United States of America, and the Department of Commerce; and Defendants-Intervenors, Allegheny Ludlum Steel Corporation, *et al*.

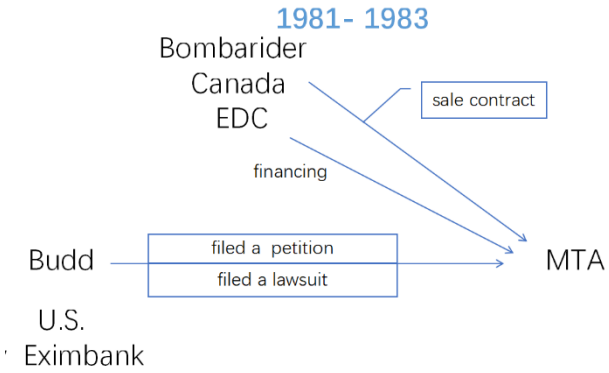
[70] Countervailing duty petitions alleging the use of subsidized export credit have been filed against the following United States imports: Ceramic Tile from Mexico, 47 Fed. Reg. 7866 (1982); Certain Commuter Airplanes From France and Italy, 47 Fed. Reg. 25,077 (1982); Railcars From Canada, 47 Fed. Reg. 31,415 (1982); Certain Commuter Airplanes From Brazil, 47 Fed. Reg. 37,309 (1982); Initiation of Countervailing Duty Investigation, Large Diameter Welded Carbon Steel Pipes and Tubes From France, 47 Fed. Reg. 24,169 (1982). Mark D. Fernald, Export Credits: The Legal Effect of International and Domestic Efforts to Control Their Use, 7 B. C. Int'l & Comp. L. Rev. 435 (1984)

[71] See Final Affirmative Countervailing Duty Determination; Ceramic Tile From Mexico and Countervailing Duty Order, 47 Fed. Reg. 20,012 (1982); and Final Affirmative Countervailing Duty Determination; Railcars From Canada, 48 Fed. Reg. 6569 (1983). Mark D. Fernald, Export Credits: The Legal Effect of International and Domestic Efforts to Control Their Use, 7 B. C. Int'l & Comp. L. Rev. 435 (1984)

especially China, to promote their export. So, this part chose such a case to analyze U.S.'s position and historical solutions to export credit.

3.4.1 Factual background

In 1981, the Metropolitan Transportation Authority, New York (MTA) solicited bids for the manufacture of subway cars for New York City's deteriorating public transportation system.[72] Four parties responded: Budd (a US producer of railcars), Bombardier (a Canadian manufacturer), Kawasaki (a Japanese railcar manufacturer), and Francorail (a consortium of French manufacturers). Part of the contract was awarded to a Japanese company, Kawasaki Heavy Industries.[73] Bids for the remaining 825 cars were requested by the MTA from Bombardier, Budd and Francorail.[74] In the end, the remaining 825 cars were awarded to Bombardier.



An important factor that influenced the MTA's decision on who got the contract of remaining 825 cars was financing.

Bombardier secured financing from the Export Development Corporation (EDC), a Canadian Crown Corporation wholly owned by the Canadian Government.[75]

The EDC agreed to finance 85% of the deal between Bombardier, Canada and MTA at an interest rate of 9.7% per annum, repayable in twenty equal semiannual installments beginning six months after completion of the shipment.[76] The MTA said that it chosed the Bombardier based on seven factors but the most important one is financing.[77] The MTA's Memorandum Regarding Selection said: "with respect to both price and financing, Bomardier offered the most

[72] Determination of the Commission in Investigation No. 701-TA 182 (Preliminary) USITC Publication 1277, at A-9, Aug. 1982.
[73] N.Y. Times, Aug. 14, 1982, at 33, col. 5.
[74] *Id.*
[75] Canadian Export Development Act, CAN. REV. STAT. ch. E-18 (1970) (amended 1981).
[76] Determination of the Commission in Investigation No. 701-TA 182 (Preliminary) USITC Publication 1277, at A-10, Aug. 1982.
[77] Determination of the Commission in Investigation No. 701-TA 182 (Preliminary) USITC Publication 1277, at A-52, Aug. 1982.

advangeous terms. Its car price was below that of Francorail's and roughly offered by Budd's. The amount of financing offered by Canada's EDC was the most favorable offer and the most impotant consideration of MTA's willingness to reward the contract to Bomardier." [78]

In early June of 1982, Budd retaliated by bringing suit in the US District Court for the Southern District of New York seeking to enjoin the procurement on the ground, inter alia, that Budd was entitled to an opportunity to seek comparable financing from the Export-Import Bank. However, his suit was dismissed.[79]

Then Budd filed a petition on behalf of the US industry producing railcars alleging that certain benefits which constitute export subsidies are being provided, directly or indirectly, to the manufacturers, producers, or exporters in Canada of railcars.[80]

The ITC preliminarily determined that a domestic industry was materially injured or threatened with material injury by reason of the allegedly subsidized import of subway car components.[81] On November 29, 1982, Commerce determined that the export credit financing and federal and provincial regional grants constituted subsidies and imposed a countervailing duty of U.S.$91 million.[82]

However, before the ITC's final determination, Budd and the unions withdrew their petition and the ITC terminated the proceeding.[83] As a result, the MTA was not required to pay any countervailing duties.

Budd withdrew its countervailing duty petition because it was satisfied with having established a precedent which will discourage other governmental units in the United States from seeking foreign governmental financing at preferential rates.[84] Besides, Budd did not want to damage irreparably relations with the MTA, an important customer, so Budd chose not to carry the investigation to its conclusion. Budd hoped that it would receive future contracts from the MTA significantly influenced its decision to withdraw its petition. [85] Subsequently, the coalition of national labor unions also dropped its complaint against the MTA in exchange for a promise by the MTA that it would not buy additional foreign-made railcars over the next three years.[86]

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[78] Determination of the Commission in Investigation No. 701-TA 182 (Preliminary) USITC Publication 1277, at A-37, Aug. 1982.
[79] Budd Co. v. Metropolitan Transp. Auth., No. 82 Civ. 3744 (S.D.N.Y. July 16, 1982) (order of dismissal).
[80] 47 Fed. Reg. 53760-53761.
[81] 47 Fed. Reg. 36042.
[82] 48 Fed. Reg. 6570.
[83] 48 Fed. Reg. 6793-94.
[84] U.S. IMPORT WEEKLY (BNA) No. 18, at 600 (Feb. 9, 1983).
[85] U.S. IMPORT WEEKLY (BNA) No. 19, at 636-37 (Feb. 16, 1983).
[86] N.Y. Times, Feb. 2, 1983, at Bl, col. 6.

In a word, out of the commercial consideration in the long term, Budd gave up its petition and the coalition of national labor unions dropped its complaint. Maybe for these corporations, imposing countervailing duties is not the most beneficial choice to compensate for the commercial loss caused by unfair competition.

3.4.2 The role of SOE in this case

In this case, the Export Development Corporation (EDC) [87], was a Canadian Corporation wholly owned by the Canadian Government. The EDC was created to help, develop and facilitate Canada's export trade within the framework of the Canadian Export Development Act by providing insurance, guarantees and direct export credits to buyers and sellers of Canadian manufacturers and services. [88]

The EDC, as a SOE of Canada, benefited the Bombardier by providing export credits, which constituted a kind of subsidy. Export credits are loans offered by an exporter, or by a private or public lending institution in the exporting country, to foreign purchasers of goods from the exporting country. EDC was such a lending institution, which gave loans to the MTA at rates well below commercial market rates constituting an advantage for Bombardier over other bidders. That's the reason why the MTA awarded the contract to Bombardier.

3.4.3 Trade tension caused by export credits provided through SOE

In the post-war era, governments began to offer export credits as a way to promote their exports of capital goods to developing countries because manufacturers and their commercial banks, however, were unwilling and unable to bear the risk of providing export credits for sales to developing countries.[89]

Governments supported export credits by offering funds to their official export credit agencies, like the Export-Import Bank of the United States [90], the Exports Credits Guarantee Department in the United Kingdom[91], the Export Development Corporation in Canada and the Compagnie Franqaise d'Assurance pour le Commerce ExtCrieur in France.[92] Then these governmental banks or companies relended money to exporters or their customers Governments offered loans at rates below

[87] The Export Development Corporation (EDC) is Canada's official export credit agency. Its purpose is to facilitate and promote export activities of Canadian companies. See Jean-Claude Cosset, Jean Roy, *The Prediction of Country Risk Classification: The Case of the Export Development Corporation of Canada.*
[88] *See infra notes 65.*
[89] UNITED NATIONS, EXPORT CREDITS AND DEVELOPMENT FINANCING 5 (1967).
[90] The Export-Import Bank of the United States (EXIM) is the official export credit agency of the United States. EXIM is an independent Executive Branch agency with a mission of supporting American jobs by facilitating the export of U.S. goods and services. *See* at https://www.exim.gov/about.
[91] The Export Credits Guarantee Department (ECGD) is a section of the Board of Trade. See F, Pi. RYDER, *Export Credit in the United Kingdom,* 933 (1981).
[92] ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, THE EXPORT CREDIT FINANCING SYSTEMs IN OECD MEMBER COUNTRES 8 (1982)

commercial rates which can help their manufacturers to compete with other foreign manufacturers in the international market, indicating that a government subsidy is provided.

Over the past decade these promotion efforts have intensified into an export credit war with nations offering export credits at rates well below commercial market rates in an effort to boost their exports.[93] The use of subsidized export credits led to trade tension among countries because it runs counter to the principle of free trade. They gave an unfair advantage to the industry that benefits from the subsidy,[94] which could distort trade and reduce world economic efficiency.[95]

3.4.4 Solution to the EDC case --- possible remedies

Countries wishing to control the use of subsidies, including export credit subsidies, have two options.[96]

First, a country that is importing a subsidized product can negate the unfair advantage caused by imposing a countervailing duty under domestic law. [97] Export credit financing at a rate below that commercially available to the recipient has been judicially determined to be a "bounty or grant" under section 1303 of the Tariff Act of 1930 of United States.[98] The usefulness of countervailing duties in controlling the use of subsidies is limited, however.[99] The trade distortions caused by subsidies are often felt in international markets. An injured exporter cannot use countervailing duties to protect itself since countervailing duties have only a domestic effect.[100]

The second option for controlling subsidies is through international agreements to limit their use. The General Agreement on Tariffs and Trade (GATT) has included rules governing the use of subsidies since its inception in 1947. In 1979, the Agreement on Interpretation and

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93 H.R. REP. No. 188,97th Cong., lst Sess. 2-3(1981); Mark D. Fernald, Export Credits: *The Legal Effect of International and Domestic Efforts to Control Their Use*, 7 B. C. Int'l & Comp. L. Rev. 433 (1984).

94 J. JACKSON, LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 755 (1977).

95 Barcelo: *Subsidies and Countervailing Duties - Analysis and a Proposal*, 9 LAw & POL'Y INT'L Bus. 779, 798 (1977).

96 J. JACKSON, LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 754-782 (1977).

97 J. JACKSON, LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 755 (1977).

98 "Subsidy" is defined at 19 U.S.C. § 1677(5) (1982) as follows:

The term "subsidy" has the same meaning as the term "bounty or grant" as that term is used in section 1303 of this title, and includes but is not limited to, the following:

(A) Any export subsidy described in Annex A to the [GATT] Agreement (relating to illustrative list of export subsidies).

(B) The following domestic subsidies, if provided or required by government action to a specific enterprise or industry, or group of enterprises or industries, whether publicly or privately owned, and whether paid or bestowed directly or indirectly on the manufacture, production, or export of any class or kind of merchandise:

(i) The provision of capital, loans, or loan guarantees on terms inconsistent with commercial considerations.

(ii) The provision of goods or services at preferential rates.

(iii) The grant of funds or forgiveness of debt to cover operating losses sustained by a specific industry.

(iv) The assumption of any costs or expenses of manufacture, production, or distribution.

99 Export Credits: *An International and Domestic Legal Analysis*, 13 LAw & POL'v INT'L Bus. 1069, 1082 (1981).

100 Mark S. Sullivan, Export Subsides: *Predatory Financing and the MTA-Bombardier Contract, 9 Brook. J. Int'l L.* 385-410 (1983)

Application of Articles VI, XVI and XXIII of the General Agreement on Tariff's and Trade (Subsidies Code) was adopted at Tokyo Round It prohibits the use of export subsidies, including subsidized export credits.[101] The Subsidies Code provides an exception from this general prohibition, however, for those government supported export credits that are granted within the terms of the Arrangement on Guidelines for Officially Supported Export Credits (Arrangement).[102]

In this case, Budd had tired to resort to the first option——imposing countervailing duties, but before the ITC's final determination, it withdrew its petition and got the settlement with the MTA.

3.5 Case study: Hydro-Quebec[103]

3.5.1 Background

On 20 December 1991, Canada requested the Committee on Subsidies and Countervailing Measures to establish a panel to examine a dispute between Canada and the United States concerning the decision taken by the United States on 23 September 1991 to initiate a countervailing duty investigation on imports of pure and alloy magnesium from Canada. After the panel was established, however, on 7 July 1993, Canada formally notified the Chairman of the panel that it had decided to withdraw its complaint, because the contract which was determined to confer subsidies in DOC's original determination was amended, and the amended contract was determined not to confer subsidies in a changed circumstance review.

The alleged contract is an electricity supply contract between the magnesium producer, Norsk-Hydro, and the provincially-owned utility, Hydro-Quebec, whose sole shareholder is the Government of Quebec[104]. Hydro-Quebec is a power company, which administered the Risk and Profit Sharing Program (RPSP). Under this program, long-term

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[101] The Illustrative List of Export Subsidies is annexed to The Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the GATT and sets out various manifestations of export subsidies. Item (K) of the List defines a subsidy as:
The grant by governments (or special institutions controlled by and/or acting under the authority of governments) of export credits at rates below those which they actually have to pay for the funds so employed (or would have to pay if they borrowed on international capital markets in order to obtain funds of the same maturity and denominated in the same currency as the export credit), or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits, in so far as they are used to secure a material advantage in the field of export credit terms.
Provided, however, that if a signatory is a party to an international undertaking on official export credits to which at least twelve original signatories to the Agreement are parties as of 1 January 1979 (or a successor undertaking which has been adopted by those original signatories), or if in practice a signatory applies the interest rate provisions of the relevant undertaking, an export credit practice which is in conformity with those provisions shall not be considered an export subsidy prohibited by this Agreement.

[102] *Id.*

[103] GATT Panel Report, United States –Measures Affecting the Export of Pure and Alloy Magnesium from Canada, SCM/174, 9 August 1993.

[104] Final affirmative countervailing duty determinations: pure magnesium and alloy magnesium from Canada. 57 F.R. 30954, July 13, 1992

contracts are signed between Hydro-Quebec and its industrial customers for the provision of electricity, among which Norsk-Hydro was such a customer.

Given that the dispute raised before GATT panel is based on a multilateral rule about the standing of petitioner for the investigation, which relates little to the SOE status, we will focus on the two contracts pertaining to the determination of subsidies. One contract is the original contract executed before the original determination("the original contract"), one is the amended contract which was determined not to confer subsidies("the amended contract").

3.5.2 The identification of subsidy provided by SOE

According to the United States Tariff Act of 1930, a subsidy will be determined if preferential condition was granted to a specific enterprise. In its final affirmative countervailing duty determination[105], i.e. the original determination claimed by Canada to GATT Panel, the DOC examined a rate discount program operated by Hydro-Quebec. Under the discount scheme, as the DOC found, the Norsk-Hydro received a preferential discount according to the terms of the contract. Norsk-Hydro received a 60 percent discount during the investigation, while other similar situated producers could only obtain a 20 percent discount during the same period. Thus, the DOC determined that Norsk-Hydro benefitted from the preferential provision of electricity and that the provision of electricity on these terms was limited to a specific enterprise, and the final affirmative determination is issued. Accordingly, the subsidies were provided by Hydro-Quebec to Norsk-Hydro.

However, the contract determined to conferring countervailable benefits was amended after the said final affirmative determination. Under the amended contract, Norsk-Hydro's electricity payments reflect fixed and variable elements, where the variable portion is a function of the relationship between Norsk-Hydro's average selling price for pure and alloy magnesium and a "target price". To determine whether the amended contract terms provide preferential benefits to Norsk-Hydro, the DOC first compared the power available to Norsk-Hydro and the maximum power available under the general rate schedule for large users, and found the amount of electricity being made available to Norsk-Hydro is so large that the rate schedule is not applicable to that company. Then the DOC decided to examine whether the price being charged to Norsk-Hydro is consistent with Hydro Quebec's standard pricing mechanism. Based on the information submitted in the changed circumstances review, the DOC found the revenue Hydro-Quebec can expect to receive under the amended contract was consistent with rate of

[105] Final affirmative countervailing duty determinations: pure magnesium and alloy magnesium from Canada. 57 FR 30950, July 13, 1992

return and rate setting principles, as a result, was consistent with Hydro-Quebec's standard pricing mechanism. Therefore, the DOC determined both preliminarily and finally that the amended contract did not confer a subsidy[106].

3.5.3 Illustration of the trade tension

In this whole case, the trade tension between or the concern of the parties is based on several issues, for example, that whether the petitioner for imposing countervailing duty can represent the domestic industry[107]. However, we will concentrate on the trade tension raised by the "SOE" status of Hydro-Quebec. Throughout the documents in this whole case, we found two comments[108] raised by the respondents in the original determination are most pertinent. We will discuss the two comments hereinafter.

3.5.3.1 Comment 14

Respondents argue that no government action was involved in the sale of electricity to Norsk-Hydro under the RPSP, and where there is no government action there can be no countervailable subsidy[109]. In response to this comment, the DOC listed four elements to support its opinion that it is correct to treat Hydro-Quebec as a government entity capable of conferring subsidies through its actions: a) the sole ownership of Hydro-Quebec owned by the Government of Quebec; b) the requisite approval by the Government of Quebec for each contract under the RPSP; c) the sitting of government officials on Hydro-Quebec's Board of Directors; d) the importance of utilization of the province's hydro-electric resources for Government of Quebec's development policies.

Besides, the DOC cited *Dutch Flowers* to show the consistency of the Department's practice. In that case, the DOC found that a utility company owned 40 percent by the Government of the Netherlands acted on behalf of the government because the Netherlands Minister of Economic Affairs reserved the right to approve selling prices and contracts[110]. It was also explained by the DOC that "while the Government of Netherlands does not own a controlling interest in Gasunie, it plays a significant role in the setting of natural gas prices[111]".

[106] Preliminary results of changed circumstances administrative reviews: pure magnesium and alloy magnesium from Canada. 57 FR 47619, October 19, 1992; Final results of changed circumstances administrative reviews: pure magnesium and alloy magnesium from Canada. 57 FR 54047, November 16, 1992
[107] SCM/130, Committee on Subsidies and Countervailing Measures, November 7, 1991
[108] 57 F.R. 30954, July 13, 1992
[109] 57 F.R. 30954, July 13, 1992
[110] 57 F.R. 30954, July 13, 1992
[111] Final affirmative countervailing duty determination: certain fresh cut flowers from the Netherlands. 52 FR 3301, February 3, 1987

In the above cases, the same issue is whether government action was involved in the actions taken by the entity wholly-or-partially owned by certain government. We noticed that, in the magnesium case, the respondents claimed the non-interference by government action, while admitting the 100 percent ownership of the Government of Quebec, to justify the contract. By contrast, the DOC in both cases enumerated several reasons more than the ownership to support its determination of subsidy. Thus, we conclude that, in the cases above, the "SOE status" did not raise concern by itself, nor did the non-controlling interests owned by the government impede the identification of subsidy. However, in such case where the subsidy was determined, the SOE was just a handy vehicle used by a government, and it is the government's actual and active intervention that led to the disputes.

3.5.3.2 Comment 16

Respondents argue that Hydro-Quebec acted in a commercially reasonable manner in negotiating its electricity contract with Norsk-Hydro. They also state that at the time of the negotiations with Norsk-Hydro, Hydro-Quebec was anticipating energy surpluses. Thus, water behind the dams would either be used to generate electricity or be wasted. Respondents state that as long as the sales price of electricity to Norsk-Hydro exceeded Hydro-Quebec's short-term marginal cost, it was commercially sound to enter into the contract. Respondents further argue that commercially justified price differentials do not constitute preferential pricing.

In response to this comment, the DOC targeted on the non-reimbursable discounts received by Norsk-Hydro. The DOC stated that it had consistently taken the position that preference results when different prices were charged to different customers. Regardless of whether price discrimination is considered commercially reasonable in any given circumstance, it still constitutes the preferential provision of the good or service[112].

In this comment, the respondents also cited *Dutch Flowers* to support its argument. We looked into that case, and found the following sentence may be what the respondents wanted to emphasis in this case:

"From the standpoint of Gasunie, it is in the commercial interest of its owners to provide greenhouse growers with gas at the zone "d" plus 0.5 guilder cents rate because this reflects the highest price Gasunie can charge without losing greenhouse customers to

[112] 57 F.R. 30954, July 13, 1992

alternative fuel sources. Therefore, the provision in the contract which stipulates the zone "d" rate plus 0.5 guilder cents per cubic meter for greenhouse growers can be justified by economic considerations and we do not consider this a preferential price.[113]"

The DOC responded to this contention as well, holding that the DOC's position in *Dutch Flowers* is correct and consistent with its practice, while the "price differentials" in the magnesium case are in a different situation. The DOC expressed in the response that, the Department's definition of preference does not require that all users pay identical price. In the case of electricity supply, where users can be categorized according to different use characteristics, a finding of no preference requires that similarly situated users pay the same rate. In *Dutch Flowers*, the prices of natural gas were broken down into five categories or zones, designated "a" through "e", where different prices were set under different zones. When a consistent rate-making "philosophy" was applied to each customer category, as the DOC stated, the same philosophy was applied to each group and no preference was exhibited towards users in any group. However, in the magnesium case, the DOC found that, regardless of the commercially reasonable consideration, or, admitting the price is commercially reasonable, the 60 percent discounts received by Norsk-Hydro was notwithstanding preferential, as similarly situated counterparts would receive some 20 percent discounts. In view of these two cases, we concluded that, it is the DOC's position that commercially reasonable price can also constitute preferential pricing when different treatments are given to different parties who are similarly situated. Thus, the commercial consideration cannot solely justify SOE's different treatments to different parties in subsides determination cases.

3.5.4 Comment to this case

Following the timeline, Canada resorted to three approaches in turn — consultation, conciliation, and suit in GATT panel — to impede the possible imposition of countervailing duties on pure and alloy magnesium from Canada, especially on the aspect of the contract reached between Norsk-Hydro and Hydro-Quebec. In the first two approaches, consultation and conciliation, Canada put forward the same claim as in the third approach, i.e. GATT dispute settlement panel, that the petitioner of the investigation lacked the standing as the representative of US domestic industry. However, since this claim was

[113] Final affirmative countervailing duty determination: certain fresh cut flowers from the Netherlands. 52 FR 3303, February 3, 1987

not supported by the US agencies, the investigation was advanced and the final countervailing duties determination was issued.

We noticed that, to bring this dispute to GATT panel, Canada invoked the lack of standing to petition for the investigation and the improper initiation of the investigation, which constituted the breach of Article 2:1 of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (the Subsidies Code). By contrast, to withdraw its complaint in GATT panel, Canada invoked the amended contract which was determined in the changed circumstance review not to grant subsidy, while accepting the legality of the initiation of the investigation. To be more specific, Canada attempted to solve this dispute in the multilateral forum, but the dispute, especially with respect to the contract, was finally solved in a more private way as amending the contract between parties. In this case, the tension raised by SOE is pertaining to the contract reached between Norsk-Hydro and Hydro-Quebec. As the latter one is an SOE, concerns such that whether government action is involved are to some extent reasonable. However, as we learned from this case, such concern can be resolved by way of tactful amending the contract, which deemed by us as a compromise. In such situation, the trade of SOE can proceed, the commercial benefits can be gained, even may not at the maximum, without determination of subsidies.

3.6 Conclusion – experiences from case studies

From the analysis of the four cases above, we conclude as follows:

3.6.1 First, the financial contribution by a government shall not specifically grant to SOEs. The specificity between SOEs and private enterprises would result in unfair advantages which incur concerns from other countries. Because SOEs benefitting from such advantages would have a competitive edge over foreign (and domestic) private competitors in home or international markets.[114]

This conclusion is easily found with the Finnish case, which is also the reason why the Finnish conduct does not be considered as subsidy. From the analysis of the facts from investigation by the US Treasury Department, the United States believe that the investment of government or state ownership is not a consideration for determining subsidies. The

[114] Kowalski, P. et al. (2013), "State-Owned Enterprises: Trade Effects and Policy Implications", OECD Trade Policy Papers, No. 147, OECD Publishing, Paris, at 5.

important reason why the case did not cause trade disputes is that the SOE in this case is not in a more favorable position compared with the private enterprises.

For another example, in the BSC case, the financial contribution (NLF) was specifically granted to BSC simply because BSC was a nationalized British company, which was determined constitute subsidies by the DOC.

3.6.2 Second, the financial contribution by SOEs granted to different enterprises shall not constitute preferential treatment. For example, the discount in Hydro-Quebec case is too obviously preferential to be determined as a fair consideration. As compared with the papermaking machine case, we can conclude that proper discount will be determined as legitimate. The government or SOE may conclude contracts by balancing the discount level with the possibility of being determined as subsidies

For another example, in the BSC case, the program, Transportation Assistance, was not determined to confer subsidies since BSC did not appear to receive preferential rates through the shipment of scrap by British Rail (another government owned company in British).

In the EDC case, export credit financing at preferential rates was determined to constitute a subsidy. The interest rate EDC offered to the Bombardier was below the commercial interest rate in the international market at that time and was determined to constitute a subsidy in U.S.'s CVD investigation. In other words, due to the preferential rates provided by EDC, the Canadian company got a preferential advantage in comparison to other countries' companies.

4 Advice for Chinese government and SOEs

4.1 From WTO to FTA: better capture SOEs?

4.1.1 GATT to SCM Agreement – the impact from identification of "public body"

The legal concept of "subsidies" was provided at Article XVI of the GATT 1947 in the GATT years. During the Tokyo Round of Multilateral Trade Negotiations in the 1970s, the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (hereinafter: Subsidies Code) was established. At that time, the legal concept of "public body" couldn't be found in the Subsidies Code.

The Agreement on Subsidies and Countervailing Measures was included in Annex 1 A of the Marrakesh Agreement Establishing the World Trade Organization. Definition of subsidy Unlike the Tokyo Round Subsidies Code, the WTO SCM Agreement contains a definition of the term "subsidy". As has been mentioned, the SCM Agreement first introduced the legal concept of "public body"[115]. How to elaborate "public body" was mentioned in several cases in the 2000s.[116] In United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China, the Appellate Body considered that the Panel's interpretation of "public body" lacks a proper legal basis, and reversed the Panel's finding, in paragraph 8.94 of the Panel Report, that the term "public body" in Article 1.1(a)(1) of the SCM Agreement means "any entity controlled by a government".[117] The Appellate Body found that "a public body within the meaning of Article 1.1.(a)(1) of the SCM Agreement must be an entity that possesses, exercises or is vested with governmental authority."[118]

On the 12th of December 2017, Mrs. Cecilia Malmström, European Commissioner for Trade, Mr. Hiroshige Seko, Minister of Economy,

[115] Article 1.1 of the SCM Agreement provides that "a subsidy shall be deemed to exist if: there is a financial contribution by a government or any public body within the territory of a Member…", Agreement on Subsidies and Countervailing Measures art. 1.1(a), Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 14 (hereinafter cited as SCM Agreement).

[116] The cases refer to:
United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China, WT/DS379;
United States – Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India, WT/DS436;
United States — Countervailing Duty Measures on Certain Products from China, WT/DS437.

[117] WTO Appellate Body Report, United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China, WT/DS379/AB/R, at para.322.

[118] WTO Appellate Body Report, United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China, WT/DS379/AB/R, at para.317.

Trade and Industry of Japan and Ambassador Robert E. Lighthizer, United States Trade Representative met in Buenos Aires, Argentine Republic and expressed their concern for the issue of SOEs.[119] The United States, Japan, and the European Union reaffirmed their concerns for the issue of SOEs in the subsequent Joint Statements on the 31st of May 2018 and on the 25th of September 2018.[120]

Moreover, the United States criticizes the Appellate Body findings on "public body" in the President's 2018 Trade Policy Agenda promulgated by the Office of the United States Trade Representative. The United States held the view that "the United States and several other Members have expressed significant concerns with a number of Appellate Body interpretations that would significantly restrict the ability of WTO Members to counteract trade-distorting subsidies provided through SOEs, posing a significant threat to the interests of all market-oriented actors."[121]

Subsequently, the interpretation of "public body" and the issue of SOEs related to the interpretation are broadly discussed nowadays. For example, the European Union expressed its attitude toward the issue of SOEs in the document, *WTO modernization Introduction to future EU proposals*. The European Union thinks that the concept of a "public body" has been interpreted in a rather narrow manner, which allows a considerable number of SOEs to escape the application of the SCM Agreement.[122] In its discussion paper, Canada holds that concerns about market-distorting effects resulted from SOEs need to be addressed.[123] It is clear that the concept of "public body" is still controversial within the context of the SCM Agreement in the WTO system.

4.1.2 USMCA: influences of the broad definition of SOE

The United States had taken the lead to promote the United States–Mexico–Canada Agreement from the second half of this year to "give (American) workers, farmers, ranchers and businesses a high-standard

[119] See the *Joint Statement by the United States, European Union and Japan at MC11*, on USTR's Press Releases, at https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/december/joint-statement-united-states , last visited on 20 Dec, 2018.

[120] See the *Joint Statement on Trilateral Meeting of the Trade Ministers of the United States, Japan, and the European Union*, on USTR's Press Releases, at https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/may/joint-statement-trilateral-meeting , last visited on 20 Dec, 2018; See the *Joint Statement on Trilateral Meeting of the Trade Ministers of the United States, Japan, and the European Union*, on USTR's Press Releases, at https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/joint-statement-trilateral# , last visited on 20 Dec, 2018.

[121] THE PRESIDENT'S 2018 TRADE POLICY AGENDA, at 23.

[122] WTO modernization Introduction to future EU proposals, WK 8329/2018 INIT

[123] Strengthening and Modernizing the WTO: Discussion Paper, JOB/GC/201, at 5

trade agreement that will result in freer markets, fairer trade and robust economic growth .. (and) will strengthen the middle class, and create good, well-paying jobs and new opportunities for the nearly half billion people who call North America home"[124]. The final text of USMCA[125] includes topics with related to state-owned enterprises.

In Annex IV, the Schedules submitted by each Party (Mexico, United States and Canada) stipulates the non-conforming activities of a state-owned enterprise or designated monopoly[126]. For instance, the Schedule of the United States mentions that, the obligation about Non-discriminatory Treatment and Commercial Considerations and Non-commercial Assistance shall be burdened by specific state-owned entities including Federal National Mortgage Association, Federal Home Loan Mortgage Corporation and the Government National Mortgage Association and so on[127].

Chapter 22 of USMCA[128] was inherited from Chapter 17 of TPP Agreements[129], of which Article 22.1[130] defines SOE as follows:

an enterprise that is principally engaged in commercial activities, and in which a Party[131]:

(a) directly or indirectly[132] owns more than 50 percent of the share capital;

(b) controls, through direct or indirect ownership interests, the exercise of more than 50 percent of the voting rights;

(c) holds the power to control the enterprise through any other ownership interest, including indirect or minority ownership; or

(d) holds the power to appoint a majority of members of the board of

[124] See the *Joint Statement from United States Trade Representative Robert Lighthizer and Canadian Foreign Affairs Minister Chrystia Freeland*, on USTR's Press Releases, at https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/joint-statement-united-states , last visited on 20 Dec, 2018

[125] The full text of USMCA can be accessed at https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/agreement-between, by each Chapter, Annex and Side Letter.

[126] See USMCA, Annex IV, under the sub-title of *Non-conforming Activities Explanatory Notes*.

[127] See USMCA, Annex IV, page IV-1 to IV-4

[128] See USMCA, Chapter 22 under the sub-title of State-Owned Enterprises and Designated Monopolies.

[129] The full text of Trans Pacific Partnership agreements can be found on USTR's official website by https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text , last visited on Dec 18, 2018.

[130] See USMCA Chapter 22, page 3-4

[131] The word "Party" here refers to any of the signing party of this agreement, typically means Mexico, United States and Canada here.

[132] For the purposes of this definition, the term "indirectly" refers to situations in which a Party holds an ownership interest in an enterprise through one or more state enterprises of that Party. At each level of the ownership chain, the state enterprise – either alone or in combination with other state enterprises – must own, or control through ownership interests, another enterprise.

directors or any other equivalent management body.

As is shown in the detailed definition given by USMCA, more often than not several important factors shall be taken into account when ascertaining the role and functions of the state, or a Party in an SOE: equity / share capital, voting rights, control through ownership interest and authority for appointment (or removal).

For the purpose of comparison, please see the table below of SOE's definitions in TPP and USMCA.

Comparison of SOE's definitions in TPP and USMCA	
TPP	USMCA
an enterprise that is principally engaged in commercial activities in which a Party:	an enterprise that is principally engaged in commercial activities, and in which a Party :
(a) directly owns more than 50 per cent of the share capital;	(a) directly or **indirectly** owns more than 50 percent of the share capital;
(b) controls, through ownership interests, the exercise of more than 50 per cent of the voting rights; or	(b) controls, through **direct or indirect** ownership interests, the exercise of more than 50 percent of the voting rights;
(c) holds the power to appoint a majority of members of the board of directors or any other equivalent management body.	(c) holds the power to control the enterprise **through any other ownership interest**, including **indirect or minority ownership**; or
N/A	(d) holds the power to appoint a majority of members of the board of directors or any other equivalent management body.

As has been highlighted, the scope of SOEs in USMCA has expanded from that in TPP agreements to have included untraditional identifications of SOEs such as "(when the state) indirectly owns more than 50 percent of the share capital". What does the expansion imply?

For the United States itself, the 18th USTR Robert E. Lighthizer[133] has claimed in his co-speech with President Trump on Oct 1[134] that, "The new agreement will include provisions in three areas that will become the **template** for the new Trump administration playbook for future trade deals"[135], and that "(we've included) a host of new provisions to combat unfair trade practices in a number of areas -- currency manipulations; new disciplines on state-owned enterprises; as well as.."[136].

For one thing, these should be some experiences worthy of reference for other countries like China in its process to create fair trade relationship with its trading partners and to fight against unfair trading acts. For another, other countries especially China, shall take into account that the broader definition of SOEs means broader range of enterprises to be regulated and to be obligated under the negative list[137]. Since "USMCA will include provisions that will become the template for trade deals",[138] more attention should be paid by SOEs and the states to comply with these provisions when SOEs get adapted to the regulation in the United States.

4.2 Competitive Neutrality: a way forward?

4.2.1 Meaning:

Competitive neutrality is the recognition that significant government business activities which are in competition with the private sector should not have a competitive advantage or disadvantage simply by virtue of government ownership and control. Competitive neutrality policy involves analysis and implementation of steps to ensure that this advantage does not occur.[139]

From the perspective of competition, the government is required to maintain a neutral attitude toward taxation, credit, subsidies, etc. For example, naturally SOEs can enjoy preferential tax breaks compared with private enterprises, obtain guaranteed low-interest loans from the

[133] See the official biography of Robert Lighthizer on USTR's website at https://ustr.gov/about-us/biographies-key-officials/united-states-trade-representative-robert-e-lighthizer, last visited on Dec 19, 2018.
[134] The whole video can the full transcript can be accessed at https://www.realclearpolitics.com/video/2018/10/01/full_speech_president_trump_touts_new_nafta_deal.html , last visited on Dec 20, 2018.
[135] See the first paragraph of his speech transcript
[136] See the paragraph of his speech transcript
[137] As discussed, Annex IV under the sub-title of *Non-conforming Activities* could be deemed as a "negative list"
[138] See the paragraph above
[139] The official definition of Competitive Neutrality could be found on https://unctad.org/en/Pages/DITC/CompetitionLaw/ResearchPartnership/Competitive-Neutrality.aspx , last visited on Nov 28, 2018

government and have direct access to government funding subsidies, etc. Competitive neutrality then, is a regulatory framework within which public and private enterprises face the same set of rules and where no entity operating in an economic market is subject to undue competitive advantages or disadvantages because of interaction with the state.

The rationale for pursuing competitive neutrality is both political and economic. The main economic rationale is that it enhances allocative efficiency throughout the economy – where economic agents (whether state-owned or private) are put at an undue disadvantage, goods and services are no longer produced by those who can do it most efficiently. The political rationale is linked to governments' role as universal regulators in ensuring that economic actors are "playing fair" (where state-owned corporate assets are concerned and vis-à-vis other market participants), while also ensuring that public service obligations are being met.

4.2.2 The history and development of Competitive Neutrality theory

Origin: The original intention of this policy occurred when government intervention had reached the level of distorting free competition in the market. The Australian government launched a reform of SOEs in the period of 1993 to improve this situation, but in vain. Therefore, the Australian government believes that it is necessary to introduce a new policy to return its competitive order to the original condition of rational allocation of resources. Moreover, the special institutional and economic background had also accelerated the emergence of competitive neutrality policies. First, Australia is a federal state composed of six independent states[140]. Each state has a high degree of autonomy, and each state has a large number of publicly owned enterprises, resulting in a regional monopoly. Secondly, although these publicly-owned enterprises had gained abundant production materials, they produced only a small amount of products. This inefficient production mode hinders the overall development of Australian economy. Therefore, the Australian government began to re-examine the rules of domestic competition law and considered it necessary to incorporate competitive neutrality policies into the competition law system.

Hilmer Report[141]: Professor Hilmer of the University of New South

[140] To avoid misunderstanding, the "state" here refers to a federated state, which means a constituent state that is part of a federal model and shares sovereignty with the federal government, instead of a country.
[141] See <National Competition Policy Review report, The Hilmer Report, August 1993-2>

Wales (NSW), was dominated as the chairman to form the National Competition Policy (NCP) Investigation Group, to investigate the implementation of the Australian competition law (Part IV of the Trade Practice Act of 1974)[142]. In 1993, the investigation team presented a research report entitled "National Competition Policy Review", aka Hilmer report. The concept of competitive neutrality then, was first proposed as part of the National Competition Policy, which is one of the best examples of federal-state co-operation. According to the Hilmer report, in April 1995, the Tasmanian Government (along with the Australian Government and all other state and territory governments) signed three inter-governmental agreements relating to the implementation of National Competition Policy. These agreements include the Conduct Code Agreement (CCA), the Competition Principles Agreement (CPA), and the Agreement to Implement NCP and Related Reforms. Separate NCP agreements were signed by the Australian Government and each of the states and territories relating to, competition payments, the Australian Government's Trade Practices Act 1974 (now the Competition and Consumer Act 2010) and competition principles.[143]

Development: The concept of competitive neutrality has gradually become an international standard advocated by developed countries through the promotion of international organizations such as OECD. In 2009, the OECD held two roundtables [144] to discuss state-owned enterprises and the principle of competitive neutrality. Between 2010 and 2012, the OECD has released several reports summarizing Australia's successful experience in promoting competitive neutrality. The 2014 United Nations Conference on Trade and Development (UNCTAD) issued a report discussing the practice of competitive neutrality in developing countries in Asia. In the basic TPP trade agreement reached in 2015, the competition neutrality also became the main content of Chapter 17 "State-owned enterprises and designated monopolies." A most notable effort made to promote competitive neutrality shall be <Competitive Neutrality: Maintaining a Level Playing Field between Public and Private Business>[145] published by OECD in

[142] The whole text of the mentioned Act can be found in <1974 Australian Trade Practice Act>
[143] See this on the Australian government's official website at https://www.treasury.tas.gov.au/economy/economic-policy-and-reform/national-competition-policy , last visited on Nov 28, 2018
[144] See details of the roundtables in <Policy Roundtables - State Owned Enterprises and the Principle of Competitive Neutrality>, accessed by http://www.oecd.org/daf/competition/46734249.pdf , last visited on Nov 28, 2018
[145] OECD (2012), Competitive Neutrality: Maintaining a Level Playing Field between Public and Private Business,

2012. Several new principles were put forward in <OECD Guidelines for Corporate Governance of State-Owned Enterprises> .[146] The widely-recognized eight principles of competitive neutrality are discuss below.

4.2.3 Building blocks of Competitive Neutrality

Under the scope of competitive neutrality set out by OECD, there're basically eight "building blocks" of competitive neutrality:

4.2.3.1 The commercial and non-commercial business activities of SOEs shall be separated. In some industries with natural monopoly characteristics, the higher the degree of separation between the commercial and non-commercial activities (such as public services), the closer to the "competitive neutrality" state. This will also promote the reduction of entry barriers in the industry and enhance the function of public services provided by state-owned enterprises. Therefore, the commercial activities and non-commercial activities of state-owned enterprises should be separated as much as possible (for example the accounting of these two activities can be done separately), and the business structure should be streamlined. Through regular review and improvement of the corresponding accountability system, the transparency of SOEs' commercial operations can be improved and competitive neutrality shall be stabilized.

4.2.3.2 The costs of any given function of commercial government shall be identified and disclosed. SOEs need to establish appropriate cost allocation mechanisms to clarify the types of businesses to which costs belong, and to separate the costs and assets of commercial and non-commercial activities. If public service obligations are subsidized by the public purse, costs should be identified in a transparent manner to ensure neither over compensation nor under compensation.

4.2.3.3 Achieving a commercial rate of return, is an important aspect in ensuring that government business activities are indeed operating like comparable businesses. If the return rate on business operations of SOEs is not required, SOEs may adjust their pricing

OECD Publishing, page 31-104.

[146] See OECD Guidelines on Corporate Governance of State-Owned Enterprises, which can be accessed by https://www.oecd-ilibrary.org/governance/oecd-guidelines-on-corporate-governance-of-state-owned-enterprises-2015_9789264244160-en , last visited on Nov 28, 2018

by lowering the rate of return, thereby gaining an unfair competitive advantage. Of course, the corresponding state-owned enterprises do not need to achieve the target rate of return for each transaction or even for each budget period.

4.2.3.4 Compensation for public service obligations imposed on public entities shall be precise and transparent. In a competitive market, state-owned enterprises will suffer some losses due to their public service functions, which are at a competitive disadvantage and may affect the quality of their public services. To compensate for this disadvantage, the state usually provides appropriate compensation. However, if excessive subsidies occur, the situation of state-owned enterprises will reverse, and the situation will be better. Therefore, the amount of compensation should be as reasonable and appropriate as possible to avoid adverse effects on the "competitive neutral" pattern as much as possible. In addition, the compensation had better be paid directly by the budgetary funds of the public sector.

4.2.3.5 Tax neutrality. In terms of taxation, state-owned enterprises and other enterprises should be treated equally. State-owned enterprises should bear similar tax burdens with its rivals in the market. An equal or equivalent treatment of public and private business activities is essential for tax neutrality.

4.2.3.6 Regulatory neutrality. To ensure competitive neutrality, government businesses should operate, to the largest extent feasible, in the same regulatory environment as private enterprises. The difference in treatment between state-owned enterprises and other enterprises should be eliminated. The preferential policies enjoyed by state-owned enterprises for providing public services must be reasonable and transparent, and policy adjustments should be made through laws and regulations when necessary.

4.2.3.7 Debt neutrality and outright subsidies. The need to avoid concessionary financing of SOEs is commonly accepted since most policy makers recognise the importance of subjecting state-owned businesses to financial market disciplines. Regardless of the source of funds, the financing costs of state-owned enterprises should be effectively controlled to ensure that they are consistent with similar levels in the market. In practice, it is believe that in

financial markets, generally the state-owned enterprises have lower default rates, resulting in lower financing costs for state-owned enterprises than competing private companies. Therefore, appropriate measures should be taken to ensure that state-owned enterprises do not benefit from explicit or implicit guarantees from the government background and enjoy lower financing rates. Factors such as employment rate shall not be taken into account when losses are long-lasting.

4.2.3.8 Public procurement neutrality. To support competitive neutrality, procurement policies and procedures should be competitive, non-discriminatory and safeguarded by appropriate standards of transparency. In reality, the economies of scale have led to long-term advantage in the operation of state-owned enterprises, which cause difficulties for competitors to enter. In addition, state-owned enterprises also have certain information advantages, so that the quotations of Chinese enterprises in the bidding process are closer to procurement needs. Furthermore, some state-owned enterprises have the competitive advantage of direct internal procurement by the department. Therefore, it is necessary to establish a strict procurement mechanism to ensure fairness in bidding and purchasing, such as establishing a complaint mechanism and corrective measures afterwards. [End]