United States – Definitive Safeguard Measures on Imports of Certain Steel Products

Comments of the United States
on Responses to Questions 48, 54, and 56
from the Panel to the Parties at the Second Meeting

January 24, 2003

Question 48

1. Korea asserts in its answer to this question that "the United States is wrong to claim that the ITC's model produces the same results as its numerical analysis and model." It argues that the ITC's COMPAS results show that a 30 percent tariff yields a 20 to 28 percent increase in import prices, while "according to the *ex post* analysis, a 30% tariff yields an 18 % increase in imports prices."[1]

2. The price-based exercise and modeling exercise presented in the U.S. first written submission "produce the same results" only in that both of these exercises confirm that the steel safeguard measures were applied less than the extent necessary to prevent or remedy serious injury and to facilitate adjustment. However, this does not suggest that these exercises (or the modeling performed by the ITC staff) yield the same numerical results.

3. For example, the figures cited by Korea are not based on the same economic model. The 18.9 percent increase in import prices (which Korea rounds down to 18 percent) was calculated according to the price-based exercise described in the U.S. first written submission and documented in Safeguard Worksheet A.[2] This figure represents the estimated degree to which import prices would have to increase for domestic producers to achieve the target operating income margin identified in our submission. Thus, it is a *goal* rather than an *estimated effect*. The other figures cited by Korea – the 20.8 to 28.0 percent range of projected increases in import prices – was the result produced by the multi-market or linked COMPAS model for a 30 percent tariff on certain carbon flat-rolled steel.[3] Thus, it is an *estimated effect* rather than a *goal*. These are clearly two different methods of analysis. The United States compared the two results solely for the purpose of showing that a tariff of 30 percent would achieve import price increases in the range required to achieve the targeted operating income margin. Comparison for any other reason, such as that suggested by Korea, is both improper and meaningless.

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[1] The Republic of Korea's Answers to the Panel's Questions for the Parties Following the Second Substantive Meeting of the Panel with the Parties, para. 74 (6 January 2003) ("Korea second responses").

[2] Paragraphs 1065 through 1080 of the U.S. first written submission describe this analysis. The relevant worksheets appear in Exhibits US-56 and US-57.

[3] Memorandum EC-Y-050 (Exhibit US-65). Since the ITC staff ran the model before the ITC issued its report, it treated only Canada as excluded from the measure.

4. Korea's argument regarding the COMPAS results generated by the ITC staff and price-based exercise in the U.S. first written submission is unclear. It could be interpreted in a variety of ways, each of which is incorrect.

5. If Korea is arguing that the COMPAS results generated by the ITC staff are different from the modeling results referenced in the price-based exercise, it is plainly incorrect. As discussed above, the price-based exercise compared an estimated import price that would achieve target operating margins with the estimated price effect of a 30 percent tariff, as reported in the ITC staff's COMPAS modeling.[4] For each product, including certain carbon flat-rolled steel, there is no difference as the exercise correctly reflected the results of the ITC staff's COMPAS modeling.[5]

6. If Korea is arguing that the estimated amount that import prices would have to increase to eliminate downward pressure on U.S. producers' prices (18.9 percent for certain carbon flat-rolled steel)[6] was a projection of the actual amount that prices would increase, it has misunderstood. The 18.9 percent figure is clearly labeled "Needed Unit value increase for non-NAFTA imports."[7] As we noted, it represents the *hoped-for* increase in import prices, and not an estimate of what will actually happen. In short, the written description of the price-based exercise and the spreadsheets in Exhibit US-56 applying that exercise do not suggest a finding that "a 30% tariff yields an 18 % increase in imports prices."[8]

7. If Korea's point is that the needed unit value increase of 18.9 percent is slightly below the low end of the range of estimated effects of a 30 percent tariff, we explained that "numerical estimates are necessarily limited in their ability to precisely quantify and isolate the full effect of imports and the appropriateness of remedial measures. . . . Numerical estimates may be useful to test whether a measure is set at an order of magnitude consistent with Article 5.1."[9] The price-based exercise demonstrates that this is the case for the safeguard measure on certain carbon flat-rolled steel, as well as the other steel safeguard measures.

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[4] First Written Submission of the United States of America, para. 1072 ("U.S. first written submission") (October 4, 2002).

[5] In this regard, the price-based exercise differed from the modeling exercise. The price-based exercise referenced the COMPAS results produced by the ITC staff, which reflect tariff levels adopted by the President, but not the exclusion of both Canada and Mexico from all products. In contrast, the modeling exercise used the same inputs as the ITC did for elasticities and for full-year 2000 data, but modeled the tariff levels and country exclusions adopted by the President. The modeling exercise also involved modeling of the change in imports during the investigation period, which the ITC did not do. U.S. Response to the Panel's Questions for the Parties at the Second Meeting of the Panel, para. 136 (January 6, 2003) ("U.S. second responses"). These differences in the use of the model would obviously change its numerical outputs.

[6] Exhibit US-56, table labeled "Weighted based on Net Commercial Sales for FLAT Products."

[7] *Ibid.*

[8] Korea second responses, para. 74.

[9] U.S. first written submission, para. 1062.

8. Finally, Korea's response to question 48 references its Exhibit 14 and certain pages of its second written submission. The Panel did not request further comments on question 50, which specifically addresses the arguments referenced by Korea, so we will not comment in this submission on the cross-referenced paragraphs.

9. We have emphasized that no numerical evaluation can be precise. We put forth the numerical exercises as conservative estimates, and not precise valuations.[10] We have also shown that a safeguard measure is consistent with Article 5.1 of the *Agreement on Safeguards* ("Safeguards Agreement")[11] if its application is *no more than* extent of the injurious effects of increased imports – the two need not be equal.[12] Thus, there is no obligation to "produce the same results" using different calculations.

Question 54

10. In paragraph 88 and footnote 83 of its responses to questions from the Panel, Korea questions why the United States used a target operating margin of 5.7 percent for the certain welded pipe industry in 2001. The United States noted in its first written submission that the ITC found that an increase in capacity for producing certain welded pipe had a "minor" negative effect on the industry in 2000.[13] Accordingly, we did not use the 2000 operating margin as a benchmark. Instead, we used the average of operating income margins in 1999 (8.1 percent) and the first half of 2001 (3.2 percent) to derive a target margin of 5.65.[14] A simple average is a conservative estimate. The 1999 margin represented 12 months of data and the 2001 margin six months. A weighted average would have resulted in a target margin of 6.5 percent.

11. The United States specifically requested the opportunity to respond to the Korean argument that we addressed in the preceding paragraph. However, the Panel's request was not so limited. Accordingly we make two additional points.

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[10] U.S. first written submission, paras. 1062 & 1079.

[11] All references in this submission to Articles are to the Safeguards Agreement.

[12] For example, the U.S. response to the first set of questions from the Panel states:

> The use of "no more than the extent necessary" indicates that Article 5.1 establishes a maximum for the application of a safeguard measure. "No more than" means that the measure may be applied up to, but not beyond, that level.

U.S. first written submission, para. 190. An additional discussion of this point appears in paragraph 101 of the U.S. oral statement at the Panel's second meeting with the Parties.

[13] U.S. first written submission, para. 1132.

[14] Since the spreadsheets in Exhibit US-56 presented operating income figures with one decimal place, this is rounded to 5.7 percent on the printout. The electronic version of the spreadsheet contains reflects the full 5.65 percent figure.

12. First, Korea criticizes the United States on the grounds that the "choices of 1996 and 1997 . . . as years prior to injury does not account for the effect of legacy costs."[15] But legacy costs were borne by the domestic industry throughout the entire period investigated. Korea also objects that no control is made for the increase in minimill capacity over the period,[16] but as the United States has already observed, the largest increase in minimill capacity was in 1997, the year chosen as the benchmark for the analysis for flat-rolled.

13. Second, Brazil objects to the fact that 1997 was a year of peak industry performance over the period and therefore cannot be representative.[17] This ignores the fact that the years 1998 through 2000 were years of even higher demand for flat-rolled products than that seen in 1997.[18] Thus 1997 was a conservative choice to use as a benchmark. It was a peak year in terms of industry performance during the period of investigation only because increased imports had negative effects on domestic prices in later years.

Question 56

14. The United States specifically suggested that the Panel allow us to present additional comments regarding paragraphs 97 and 98 of Korea's responses to question 56. We will structure our comments around the text of those responses.

Korea's assertion that "[t]o comply, there should be a finding that the industry is able to adjust to import competition and that it has a plan for doing this." (para. 97)

15. To begin, nothing in the Safeguards Agreement requires that an industry present an adjustment plan, or that the competent authorities (or the Member itself) determine that the industry is "able to adjust." Article 4.2(a) is specific about what the competent authorities *must* consider – "all relevant factors of an objective and quantifiable nature having a bearing on the situation of the industry." The Article establishes this obligation as part of the "investigation to determine whether increased imports have caused or are threatening to cause serious injury." It does not mention the facilitation of adjustment. Thus, the "relevant" factors are those relating to injury or causation. The industry's ability to adjust to import competition (or any industry adjustment plans) do not advance this inquiry and, therefore, are not "relevant" in the sense of Article 4.2(a).

16. Article 5.1 addresses imposition of safeguard measures, and does not require the consideration of specific factors. Therefore, it does not obligate a Member to address the industry's ability to adjust, or to require an adjustment plan from the domestic industry. Indeed,

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[15] Korea second responses, para. 87.

[16] Korea second responses, para. 86.

[17] Response of Brazil to the Panel's Questions for the Parties, question 54 ("Brazil second responses") (6 January 2003).

[18] "By any measure, the period of investigation saw significant growth in U.S. demand for certain carbon flat-rolled steel." *Steel*, Inv. No. TA-201-73, USITC Pub. No. 3479, p. 56 (December 2001) ("ITC Report").

reading the Safeguards Agreement to require the industry as a whole to agree on what adjustment efforts to undertake would suggest the existence of a requirement to create cartels or an endorsement of collusion among the domestic producers. Nothing in the Safeguards Agreement supports such a conclusion.

17. Nonetheless, Korea asserts that "[t]o comply," a Member should make "a finding that the industry is able to adjust to import competition and that it has a plan for doing this."[19] It is unclear exactly what provision Korea sees as requiring such compliance. Paragraph 96, which immediately precedes this assertion, notes that Article 7.2 requires evidence that the industry "is adjusting," and Article 7.4 requires progressive liberalization of the measure "in order to facilitate adjustment."[20] Korea does not explain how either of these obligations is relevant to the initial decision whether and to what extent to apply a safeguard measure. Indeed, Article 7.2 envisages an analysis of the effectiveness of the measure *after* it has been in place, which a Member surely cannot perform before applying the measure. Article 7.4, which is not subject to a claim raised by any of the Parties, addresses the reduction in the level of application of a measure after its initial application. It is difficult to imagine how this provision would be applicable to the decision on the initial level of application of a measure, as opposed to any subsequent reductions in application. In any event, an adjustment plan or pre-application findings regarding adjustment are not necessary for a Member to determine at a later date whether adjustment has occurred. Thus, a Member is not obligated to seek an industry adjustment plan or to make a finding that the industry is "able to adjust" in order "to comply" with Articles 7.2 and 7.4.

18. In paragraph 95, which precedes the discussion of Article 7, Korea asserts that "to facilitate adjustment" in Article 5.1 means that "the industry must be in a position to compete with imports after the relief ends" and that "'the temporary breathing room' provided by safeguards must be used to adjust to increased import competition."[21] These statements mistake the objective of a safeguard measure – to facilitate the domestic industry's adjustment to import competition – for an obligation. A Member cannot guarantee in advance that a safeguard measure will achieve a full adjustment to import competition. Other forces could frustrate the success of a measure.

19. Korea's interpretation would also disregard the word "facilitate." As the EC and Brazil point out, "facilitate" means "make easy or easier; promote, help forward (an action, result, etc."[22] Further, according to the EC, "it therefore implies a contribution to a result – not the

[19] Korea second responses, para. 97.
[20] Korea second responses, para. 96.
[21] Korea second responses, para. 95.
[22] Replies by the European Communities to the Questions of the Panel at its Second Substantive Meeting, para. EC-116 (6 January 2003) ("EC second responses"), quoting the New Shorter Oxford English Dictionary (electronic version) (January 1997). Brazil raises a similar point in its response to question 56.

assurance of a result."[23] Thus, Article 5.1 cannot be interpreted to require a Member to ensure before taking a safeguard measure that the industry will be able to compete with imports after termination of a safeguard measure.

20. Therefore, Article 5.1 does not support Korea's view that a Member should require the domestic industry to submit an adjustment plan, and make a finding that the industry is able to adjust. Articles 5.1, 7.2, and 7.4 are the only provisions of the WTO covered agreements that appear in Korea's response. Since they do not support Korea's argument, the Panel should reject it.

21. Finally, although Article 5.1 does not require adjustment plans, or analysis of the industry's ability to adjust, the U.S. safeguard statute envisages the submission of adjustment plans by domestic producers.[24] Many of the domestic producers of the ten products subject to steel safeguard measures submitted plans. In addition, the ITC asked producers to indicate what actions they would take to adjust to import competition. Producers provided this information primarily in the form of company-specific (and generally confidential) objectives.[25]

Korea's assertion that "*both *requirements of Article 5.1 (first sentence) limit the permissible extent of relief." (para. 97)

22. The United States addressed this issue in its response to this question, which appears in paragraphs 185 through 186 of the responses to the Panel's second set of questions.

Korea's assertion that "there is no record evidence or even evidence presented to the Panel by the United States which explains how relief was necessary to allow for adjustment at all, let alone to adjust to increased* imports *alone. (para. 98)

23. The record does contain such evidence. For certain carbon flat-rolled steel, hot-rolled bar, cold-finished bar, rebar, certain welded pipe, FFTJ (fittings, flanges, and tool joints),

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[23] EC second responses, para. 117. Brazil makes a similar point in its response to question 56. The United States agrees with this interpretation of "facilitate." (Indeed, paragraph 1025 of the U.S. first written submission cited the definition.) However, we disagree with the conclusion by the EC and Brazil that this means that a Member's ability to facilitate the adjustment to import competition is delimited by the need to prevent or remedy serious injury. If "making easier" or "promoting" adjustment to the injurious effects of imports (as distinguished from the effects of other factors having injurious effects) requires application of a measure beyond the extent of remedying the injurious effects of imports, Article 5.1 would permit such a measure.

[24] Section 202(a)(4) of the Trade Act of 1974, 19 U.S.C. § 2252(a)(4) ("A Petitioner under paragraph (1) may submit to the Commission and the United States Trade Representative . . . either with the petition, or at any time within 120 days after the date of filing of the petition, a plan to facilitate positive adjustment to import competition."). Of course, the fact that the U.S. statute – independent of the Safeguards Agreement or Article XIX of the *General Agreement on Tariffs and Trade 1994* envisages adjustment plans does not elevate them to the status of an international obligation.

[25] A summary of these plans appears on pages 361-362, 374, 382, 389, 396, 403, and 412 of the ITC Report. Tabulations of proposed adjustment efforts appear on pages FLAT-78, LONG-102 - LONG-103, TUBULAR-66, and STAINLESS-91 of the ITC Report.

stainless steel bar, and stainless steel rod, the ITC majority found that imports undersold domestic products, and that this condition had a negative effect on domestic producers' prices.[26] The ITC found further that declining prices contributed to declining profitability. Finally, the ITC found that the domestic industries' capital and research and development efforts were impaired. For each of the products, data on import volumes and values indicate that foreign producers were willing and able to increase greatly their sales of these low-priced products.

24. The mechanism for the suppression and depression of prices is obvious. When increased imports sell for prices lower than comparable domestic products, purchasers can switch to lower priced imports. The threat of losing sales can force domestic producers to lower their prices. As long as imports remain in the market at prices lower than comparable domestic products, it is difficult or impossible for domestic producers to improve their situation by raising prices. By demonstrating that imports can increase dramatically, a recent surge would give credibility to customers' threats to replace domestic sales with imports, and would increase their ability to obtain pricing concessions.

25. The effect on the industry's ability to adjust is equally obvious. An industry with low or negative profitability cannot attract the funds necessary to pay for adjustment. Banks will not lend and investors will not contribute capital needed to restructure, to buy more efficient equipment, to retrain workers, or to take any other steps that would facilitate adjustment.

26. It is beyond dispute that application of the safeguard measures would facilitate the industry's adjustment. An increase in the price for imports would lessen their negative effect on domestic producers' prices, which would likely boost profitability. The data in the ITC record demonstrate that, at least in the first half of 2001, market conditions were not such that import prices would rise sufficiently by themselves. A safeguard measure would bolster import prices and relieve pressure on domestic producers' prices. No party suggested an alternative means to increase domestic and import prices. Thus, the safeguard measures were necessary both to raising domestic prices and thereby providing the funds that would facilitate adjustment.

27. There should be no concern that the tariff measures applied by the United States would also address the effects of other causes that putatively had a negative effect on the various industries. For example, they would not eliminate excess capacity, revive flagging demand, or address problems allegedly faced by particular producers, among other things. Thus, it is clear that the steel safeguard measures will facilitate the industry's adjustment to import competition.

Korea's assertion that "[t]he United States has even denied that adjustment was a consideration in establishing the level of relief." (para. 98)

28. This assertion represents something of a reversal, in that Complainants had previously argued that the United States was focusing on the need to facilitate adjustment, and disregarding

[26] ITC Report, pp. 61-62, 97, 106, 113, 163, 176, 211, and 220-221.

the prevention or remedy of serious injury.[27] The only support Korea cites for its exactly opposite characterization of the U.S. position is paragraph 119 of the U.S. second oral statement.[28] That paragraph states:

> As we noted in our first written submission, our numerical exercises are based solely on remedying the injurious effects of increased imports as identified by the ITC, and do not assert that adjustment to import competition required application of a safeguard measure *beyond that extent*. (emphasis added).

But Korea ignores the preceding paragraph, which states:

> It is also clear that the concepts of remedying serious injury and facilitating adjustment overlap to a degree. "Rectifying" or "making good" the injurious effects of increased imports will provide the industry with resources that will enable it to compete more successfully with imports upon termination of the safeguard measure. Indeed, that is the purpose of a safeguard measure – to provide temporary breathing space so the industry *can* adjust.[29]

29. These two paragraphs reflect that the United States *did* consider the need to facilitate adjustment to import competition in deciding to apply the steel safeguard measures. This has been clear from the outset. In Proclamation 7529, which established the measures, the President "determined that these safeguard measures will facilitate efforts by the domestic industry to make a positive adjustment to import competition."[30] These two paragraphs also reflect the point that the United States *did not* consider in this proceeding the need to facilitate adjustment as a factor indicating that any of the steel safeguard measures should be applied *beyond* the extent necessary to prevent or remedy the injurious effects attributable to increased imports.

30. We have shown that under Article 5.1, preventing or remedying serious injury and facilitating adjustment are additive bases for a safeguard measure. Therefore, our discussion of Article 5.1 has focused on confirming that the steel safeguard measures were applied no more than the extent necessary to prevent or remedy serious injury. This was also the focus of the Appellate Body's analysis in *US – Line Pipe*.[31] It is our view that remedies applied within this

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[27] Second Written Submission of the European Communities, para 509 (26 November 2002) ("The only indication we had in the Presidential Proclamation of the purpose sought to be achieved by the US safeguard measures is that they were designed to facilitate efforts by the domestic industry to make a positive adjustment to import competition and provide greater economic and social benefits than costs."). The EC expands on this allegation in paragraphs 510 through 512 of that submission.

[28] Korea second responses, para. 98, note 86.

[29] Oral Statement of the United States at the Second Meeting of the Panel with the Parties, para. 118 (10 December 2002).

[30] Proclamation 7529 of March 5, 2002, 67 Federal Register 10553, 10555, recital 14 (March 7, 2002).

[31] *United States – Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea*, WT/DS202/AB/R, adopted 8 March 2002, paras. 237-262. Indeed, Norway recognizes that the Appellate Body did not address the role of facilitating adjustment in the Article 5.1 analysis. Norway, Second

limitation, like each of the steel safeguard measures, will be equally necessary to facilitate adjustment. Thus, there was no need for a further inquiry in this dispute into whether facilitating adjustment would justify applying one of the measures at a higher level. This in no way suggests that the steel safeguard measures, which were applied at or below the level necessary to prevent or remedy serious injury, would not facilitate adjustment.

Response to Panel Questions, question 56.