PROPOSED AMENDMENTS TO THE COUNTERVAILING DUTY LAW

HEARING

BEFORE THE

SUBCOMMITTEE ON TRADE

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

NINETY-EIGHTH CONGRESS

FIRST SESSION

OCTOBER 20, 1983

Serial 98–54

Printed for the use of the Committee on Ways and Means

U.S. GOVERNMENT PRINTING OFFICE

28-466 O WASHINGTON : 1983

COMMITTEE ON WAYS AND MEANS

DAN ROSTENKOWSKI, Illinois, *Chairman*

SAM M. GIBBONS, Florida
J. J. PICKLE, Texas
CHARLES B. RANGEL, New York
FORTNEY H. (PETE) STARK, California
JAMES R. JONES, Oklahoma
ANDY JACOBS, JR., Indiana
HAROLD FORD, Tennessee
ED JENKINS, Georgia
RICHARD A. GEPHARDT, Missouri
THOMAS J. DOWNEY, New York
CECIL (CEC) HEFTEL, Hawaii
WYCHE FOWLER, JR., Georgia
FRANK J. GUARINI, New Jersey
JAMES M. SHANNON, Massachusetts
MARTY RUSSO, Illinois
DON J. PEASE, Ohio
KENT HANCE, Texas
ROBERT T. MATSUI, California
BERYL ANTHONY, JR., Arkansas
RONNIE G. FLIPPO, Alabama
BYRON L. DORGAN, North Dakota
BARBARA B. KENNELLY, Connecticut

BARBER B. CONABLE, JR., New York
JOHN J. DUNCAN, Tennessee
BILL ARCHER, Texas
GUY VANDER JAGT, Michigan
PHILIP M. CRANE, Illinois
BILL FRENZEL, Minnesota
JAMES G. MARTIN, North Carolina
RICHARD T. SCHULZE, Pennsylvania
BILL GRADISON, Ohio
W. HENSON MOORE, Louisiana
CARROLL A. CAMPBELL, JR., South Carolina
WILLIAM M. THOMAS, California

JOHN J. SALMON, *Chief Counsel*
JOSEPH K. DOWLEY, *Assistant Chief Counsel*
ROBERT J. LEONARD, *Chief Tax Counsel*
A. L. SINGLETON, *Minority Chief of Staff*

SUBCOMMITTEE ON TRADE

SAM M. GIBBONS, Florida, *Chairman*

DAN ROSTENKOWSKI, Illinois
JAMES R. JONES, Oklahoma
ED JENKINS, Georgia
THOMAS J. DOWNEY, New York
DON J. PEASE, Ohio
KENT HANCE, Texas
CECIL (CEC) HEFTEL, Hawaii
MARTY RUSSO, Illinois

GUY VANDER JAGT, Michigan
BILL ARCHER, Texas
BILL FRENZEL, Minnesota
RICHARD T. SCHULZE, Pennsylvania
PHILIP M. CRANE, Illinois

DAVID B. ROHR, *Professional Staff*
MARY JANE WIGNOT, *Professional Staff*
RUFUS YERXA, *Professional Staff*
ANN FLAIG DULANEY, *Professional Staff*
FRANKLIN C. PHIFER JR., *Professional Staff*

CONTENTS

SUBMISSIONS FOR THE RECORD

PROPOSED AMENDMENTS TO THE COUNTERVAILING DUTY LAW

THURSDAY, OCTOBER 20, 1983

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON TRADE,
Washington, D.C.

The subcommittee met at 9:10 a.m., pursuant to notice, in room 1100, Longworth House Office Building, Hon. Sam M. Gibbons (chairman of the subcommittee) presiding.

[The press release announcing the hearing follows:]

[Press release of Wednesday, Oct. 12, 1983]

HON. SAM M. GIBBONS (D., FLA.), CHAIRMAN, SUBCOMMITTEE ON TRADE, COMMITTEE ON WAYS AND MEANS, U.S. HOUSE OF REPRESENTATIVES, ANNOUNCES A HEARING ON PROPOSED AMENDMENTS TO COUNTERVAILING DUTY LAW ON OCTOBER 20, 1983

The Honorable Sam M. Gibbons (D., Fla.), Chairman of the Subcommittee on Trade of the Committee on Ways and Means, U.S. House of Representatives, today announced that the Subcommittee will hold a public hearing to consider various proposed amendments to the countervailing duty law designed to address the problem of two-tiered pricing schemes established by foreign governments on natural resources. The hearing will be held on Thursday, October 20, 1983, beginning at 9:00 a.m. in the main Committee hearing room, 1100 Longworth House Office Building. Testimony will be received from invited witnesses only.

The problem of foreign government regulatory controls affecting natural resource distribution is one of growing concern to U.S. industries. These policies, which are becoming particularly noticeable in the energy sector, generally involve a rigidly controlled high world price for the resource coupled with a domestic price that is a mere fraction of the world price. Such policies are being pursued by a number of resource-rich countries to promote their own export industries and, in the process, may be causing material injury to resource-based manufacturers in the United States.

The hearing will allow interested parties an opportunity to discuss whether and to what extent such policies should be treated as subsidies, and to comment upon various alternative approaches to this problem which have emerged during the Subcommittee's consideration of comprehensive reforms in our antidumping and countervailing duty laws. The alternatives in question would all authorize a countervailing duty against imports of a resource-based product if the resource is the subject of a government price control scheme which sets a lower price for dometic use than for exportation. All three alternatives would require a finding that the controlled resource constitutes a significant portion of a resulting product's manufacturing cost and that exports of the resulting product are causing material injury to U.S. producers of the like product. However, they differ as to the measurement of the subsidy level. The three possible measurements are:

1. The difference between the controlled domestic price and the export price.
2. The difference between the controlled domestic price and the lower of the export price or the price generally available to U.S. producers.
3. The difference between the controlled domestic price and the "fair market value," which would be determined by an assessment of the following factors: (a) the generally available world price, (b) the average price to U.S. producers, (c) produc-

tion costs and the extent to which they bear a reasonable relationship to the world price, and (d) the degree of price suppression in the domestic market caused by the government regulation.

Any interested person or organization may file a written statement for inclusion in the printed record. Persons submitting a written statement should submit at least six (6) copies by the close of business, Thursday, October 20, 1983, to John J. Salmon, Chief Counsel, Committee on Ways and Means, U.S. House of Representatives, Room 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements for the record of the printed hearing wish to have their statements distributed to the press and the interested public, they may submit 100 additional copies for this purpose if provided to the full Committee office during the course of the public hearing.

Chairman GIBBONS. Good morning, ladies and gentlemen.

As all are aware, this is a public hearing of the Trade Subcommittee of the Ways and Means Committee. We welcome each of you here today and look forward to hearing your testimony.

Today's hearing is to receive testimony on the so-called natural resource provision which is being considered by the subcommittee in the context of our proposed Trade Remedies Reform Act. As most of you know, the subcommittee has considered several optional approaches to this issue, which are summarized in our press release announcing this hearing.

Today we hope to concentrate our attention on this matter and develop a solution. We hope to hear from Members of Congress and we will hear them first. We have received written testimony from Senator Domenici and from Congressman Gillis Long, both of whom are unable to attend the hearing today. Their statements will be a part of our record.

[The prepared statements of Senator Domenici and Congressman Long follow:]

STATEMENT OF HON. PETE V. DOMENICI, U.S. SENATOR FROM THE STATE OF NEW MEXICO

I very much appreciate the opportunity to testify before your subcommittee today, Mr. Chairman, and I congratulate you and the other members of this subcommittee for taking the initiative on the countervailing duty law designed to address the problem of two-tiered financing schemes established by foreign governments on natural resources.

The upstream energy subsidies that you are discussing today have been a menace for years. The domestic nitrogen producers and more recently the carbon black and domestic cement industry have been harmed unfairly by these subsidies. However, the potential is there to become a problem for the entire petrochemical industry and every energy-intensive industry competing with a government-owned monopoly using artificially low-priced energy to promote exports.

I am most familiar with the cement industry so I will focus my remarks on their situation.

In recent years, a disturbing development has emerged in the cement industry. Increasingly, foreign producers located in countries with large reserves of natural gas and oil have been aggressively entering the energy intensive industries such as cement production. These same countries have nationalized their natural resources and have created state-owned monopolies to produce and distribute energy. They have made it a national priority to increase capacity of their energy-intensive manufacturers like cement, ammonia, and steel. They have made it a national priority to promote the export of such commodities. They can virtually guarantee whatever share of our U.S. market they want by selling arbitrarily low-priced energy produced by their government-owned and controlled producers to their cement, ammonia and steel producers.

Let me use Mexico as an example because Mexican cement is a particulary troublesome competitor in New Mexico as well as the rest of the Southwest and Florida. Moreover, this is potentially a problem for any energy intensive industry faced with competing with a government-owned monopoly which provides the competition with basic raw materials on a virtually cost-free basis.

Cement manufacturing is a highly energy-intensive process. Energy constitutes about one-half of the direct cost of manufacturing cement. Cement has one of the highest ratios of energy costs to total material costs of all manufactured products. Natural gas and oil are the principal components used in the production of cement. Unfortunately for the international trading system—and especially the U.S. markets—in Mexico, PEMEX is the special government entity which owns and controls production and sale of natural gas and oil. PEMEX sells Mexican cement companies "combustoleo Pesado", a heavy fuel oil at $1.23 per barrel—assuming a Ps 150 per $1 exchange rate. An unsubsidized cost of fuel needed to produce a ton of cement is $14.96 per ton; the subsidized cost for Mexican cement is $0.68. Even using the most modern technology, U.S. cement producers cannot hope to compete effectively against Mexican cement which benefits from a subsidy estimated by some of my constituents to be $20.36 per ton. $1.23 per barrel, that's the arbitrary price the Mexican government has decided to sell heavy fuel oil to its cement producers. That's an artificially low price and that's the unfairness.

This is a classic example of unfair foreign government subsidization of a domestic industry with direct and substantial impact on the United States. It involves precisely the kind of practice that our countervailing duty laws should address, but apparently they do not.

The cement industry tried to use our trade laws to correct this meddlesome and market disrupting practice. Their lawyers established a compelling case before the Commerce Department. The Final Affirmative determination did not take into account the energy subsidy in spite of the uncontroverted facts. The cement industry did win a countervailing duty equal to about 6 percent industry-wide. This 6 percent was allowed because of several other Mexican Government programs, mostly tax credits, immediate depreciation and below market rate financing. That 6 percent countervailing duty looks puny when compared with a 50 pecent energy subsidy. It looks to me like a slight inconvenience or just another insignificant cost of doing business. It certainly isn't fairness.

The Commerce Department representatives tell me that to recognize and to impose countervailing duties against such upstream energy subsidies the law needs to be changed. I understand that you are considering three possible approaches to measure the subsidy level for the purpose of imposing countervailing duties.

I would think that either of the first two approaches would correct the problem. The first approach would calculate the countervailing duty based on the difference between the controlled domestic price and the export price.

The second approach uses the difference between the controlled domestic price and the lower of either the export price or the price generally available to U.S. producers. I understand that this approach has been proposed to guard against such situations as the bad bargain/change of circumstances possibility. This is the situation we have with some Mexican natural gas right now. Several years ago we agreed to buy natural gas from Mexico at $4.60 per MCF. This price was agreed upon based on our belief that the price of oil and natural gas would continue to increase. Because this has not happened we are buying gas at $4.60 per MCF, but the price generally available to U.S. producers is $2.80 to $3.

I would caution against the type of approach suggested in the third alternative. This formula for determining the appropriate countervailing duty takes the difference between the controlled domestic price and the "fair market value", which would be determined by an assessment of the following four factors: the generally available world price; the average price to U.S. producers; production costs and the extent to which they bear a reasonable relationship to the world price; and the degree of price suppression in the domestic market caused by government regulation.

I don't find either of these two criteria troublesome. However, I do have some concerns about the third and fourth criteria.

I have spent years on the Senate Energy and Natural Resources Committee and the third criteria, production cost and the extent to which it bears a reasonable relationship to the world price, I feel is of questionable value in setting a standard for countervailing duty relief. I can tell you, as will any producer in the natural resource field, that the cost of production does not always logically compare to the value of the product or the world price.

I am also concerned about the feasibility of the fourth criteria. The degree of price suppression in the domestic market caused by government regulation, may be difficult, if not impossible to determine with any certainty or reliability.

These are a few of my thoughts on these three possible formulas. I am sure that the hearing today will give us all a better idea regarding the appropriate measure. I am sure that the subcommittee will arrive at a workable formula.

I can't stress how important this issue is. I think we are seeing just the beginning of what I consider to be a desperate effort on the part of other governments to capture U.S. markets and to earn foreign currency to service their external debt.

Only a year ago Mexico was in the headlines because of the state of its economy, the devaluations of its currency, its unemployment and the specter of default on its loans. Those problems have not disappeared.

A recent 1981 study on Mexican energy policies makes it clear that the explicit policy of undervaluing oil and gas and other energy resources, has artificially reduced PEMEX revenues and has forced PEMEX and Mexico to borrow excessively, creating inflation and devaluation of the peso.

There are those who may say that it is none of our business how Mexico chooses to use its natural resources. However, Mexico's energy pricing practices are disrupting U.S. markets and I believe that the ramifications are potentially far reaching. Right now we are hearing about our U.S. producers seeing their customers lured away. I think that the imprudent pricing of these valuable natural resources will result in continued economic ills for Mexico. At the same time the U.S. will lose reliable and efficient domestic industries.

I have already seen the symptoms of this in my own state. New Mexico presently has only one cement plant near Albuquerque. Another plant, in El Paso has provided a substantial amount of cement to my state's market. That plant was built in 1910 and was scheduled to be replaced by another modern plant near Las Cruces. The project is on hold. The President of the company has told me that the unfair competition from subsidized Mexican cement is shrinking the Southwest's market and is severely and adversely affecting the prospects for that plant.

This plant would mean employment for 400 people during the three year construction phase of the project. Additional jobs would be generated because of the need to construct railroad spurs, service roads and electrical facilities. Approximately 150 hourly and salaried personnel would be required to operate the plant with a total annual payroll exceeding $4.5 million. In addition, the plant would consume a number of products and utilize significant services that would be provided from within the state including:

Approximately 100,000 tons of New Mexican coal at an annual cost of approximately $5 million;

Approximately 120,000 megawatt hours of electricity at an estimated annual cost of $6 million;

Railroad and truck freight at an estimated annual cost of $10 million; and

Gypsum, iron ore, aluminum materials, operating and maintenance supplies at an estimated annual cost of $1.9 million.

Because of the enormous capital cost involved with the construction of such a plant, it is essential that the producer be assured that it can operate consistently at a fairly high level of capacity before the project is approved. Expanding exportation of Mexican cement not only debases the price of cement in the market, but more importantly, reduces the potential market that the new plant can service.

I have talked about cement and energy today, but this is only one element of a larger problem of how to conduct international trade when other governments insist on upstream energy subsidies and other types of market disrupting practices which are inconsistent with free and fair trade and which undercut our domestic producers.

Unless Congress does something to restore competitiveness and fairness to this sector of the economy the needed revitalization of our industries may not take place.

I have given you one example. There are many, and for this reason I hope you will act quickly to report out a trade remedy bill that has a strong and effective provision addressing the problem of upstream energy subsidies.

Thank you, Mr. Chairman.

Statement of Hon. Gillis W. Long, a Representative in Congress From the State of Louisiana

I am grateful to the Chairman of the Trade Subcommittee, Congressman Sam Gibbons, for scheduling today's hearing on this important issue. I am delighted to see that my bill on petrochemical imports, H.R. 3801, has generated so much interest and discussion. For nearly a year now I have been warning that the future of the U.S. petrochemical industry is jeopardized by subsidized imports from some of the energy-rich countries. Many others seem to share my concern and we now can focus on what we can and should do to meet this challenge.

After a decade of growth and prosperity, the U.S. petrochemical industry faces a period of painful adjustment. Many feel that this industry is beginning a long period of decline. There is a worldwide excess in production capacity for many petrochemicals, exports and domestic sales are off due to the worldwide recession, and the over-valued dollar is hurting all U.S. exporters. The painful transition facing the U.S. petrochemical industry is just beginning and it will occur no matter what action this Congress takes on trade law reform.

There is, however, no way even the most efficient U.S. petrochemical plant can compete in either the U.S. or in the world market if foreign governments are permitted to blatantly subsidize their growing petrochemical industries. We may not have much control over the other problems facing this important industry but we can take action to ensure that foreign governments do not exacerbate the situation by conferring a contrived and unfair advantage on their own petrochemical producers. How we respond to this challenge will have a major bearing on the extent to which petrochemicals will continue to be produced in this country. It will affect thousands and thousands of jobs in many regions of the country.

The key inputs in production of petrochemicals, of course, are petroleum and natural gas. When a foreign government supplies these key production inputs to their petrochemical plants at a fraction of the world market price, the petrochemicals themselves can be produced at a fraction of the costs of production for U.S. producers. Indeed, this discount price for the key production inputs permits foreign petrochemicals producers to cut their production costs to one-fifth or even one-tenth those of other petrochemical producers, like those in this country, which must buy their petroleum and natural gas inputs at world market prices.

No discrimination would be involved and no unfair advantage would be conferred by this subsidy if these foreign governments were willing to sell oil and natural gas to U.S. producers at the same discount price. But, of course, they won't do this. They set one low price for the oil and natural gas they supply to their own producers and set another, much higher market price for all other customers. This two tier pricing system gives a preferential price only to the country's domestic industries.

That this two tier pricing system for energy confers a subsidy couldn't be more obvious. If the foreign petrochemical producers had to obtain oil and natural gas feedstocks from any supplier other than their own government, they would be forced to pay world market prices, just as do U.S. producers. The only reason these foreign producers can obtain oil and natural gas at a discount price is because their governments are willing to subsidize the price. Indeed, these governments are quite honest about the intent of this practice; it is designed to give their domestic producers an advantage in exporting to other countries where the producers receive no subsidy.

The effect of this government subsidy is exactly the same as if the government simply gave each petrochemical plant a cash grant with which it could purchase oil and natural gas. The subsidy is blatant and it gives foreign petrochemical producers an insurmountable and unfair advantage in international trade.

The Commerce Department has argued in two cases involving petrochemical imports that two tier pricing of energy inputs does not confer a subsidy if the foreign government is willing to supply its oil and natural gas feedstocks at a discount price to more than one industry within the country, not just to one industry like petrochemicals. To me this rationale is non-sense. When a foreign government supplies a key production input at preferential prices to more than one of its domestic industries, it is subsidizing each of these industries. A subsidy does not cease to be a subsidy because it is produced to more than one beneficiary—particularly when in each case the subsidy dramatically reduces production costs. In addition, the Commerce Department argues that it makes no difference that the government is unwilling to give the preferential price to U.S. companies which wish to purchase the oil and natural gas. This conclusion just adds insult to injury. The Department's view on this issue is myopic and is a strained interpretation of the current countervailing duty statute.

While it is easy enough to understand the nature of the subsidy that is conferred by a two tier pricing system for energy, there are legitimate questions about how to measure the extent of the subsidy and how to provide an adequate remedy for injured U.S. producers. In H.R. 3801 I have proposed comparing the price at which the foreign government supplies the energy to its producers and the price at which such energy is generally available to U.S. producers. Others would compare the subsidized price to the export price set by the same government for the same commodity.

A natural compromise between these two alternatives would be to compare the subsidized price to the lower of the price generally available to U.S. producers and the government-set export price. This synthesis would give foreign governments every incentive to reduce or eliminate the subsidy or to lower their export price and it would give U.S. producers an incentive to seek the lowest price energy available in the United States. Chairman Gibbons' leadership in fashioning an appropriate and effective remedy for two tier pricing has been outstanding and I am happy to work with him in resolving this issue.

In fashioning an effective remedy for the problem of two tier energy pricing, we must make sure that we do not unintentionally undermine investments that U.S. petrochemical producers already have made abroad, particularly in the Middle East. H.R. 3801 would not cover imports from countries that do not maintain a two tier pricing system or which are willing to supply oil and natural gas to U.S. companies at the same price as these commodities are supplied to their domestic producers. This exemption is extremely important in avoiding any possibility of fostering retaliatory actions against U.S. producers. This exemption also means that U.S. consumers of petrochemicals will still be able to obtain petrochemicals at the lowest market price. It would only cover petrochemicals the price of which does not reflect the fair market cost of production due to an unfair government subsidy. This is a fair trade-off that balances the concerns of both U.S. producers and consumers of petrochemicals.

The economic stakes in this effort to deal with two tier pricing are immense. There are some who see the U.S. petrochemical industry as the next auto or steel industry. Others see it as inevitable that most petrochemicals will be produced in the energy-rich countries, with U.S. producers able only to preserve a niche in specialty petrochemicals. But think about what this would mean. In Louisiana alone we have invested $35 billion in petrochemical plants and these plants employ more than 30,000 people. Indirectly the petrochemical industry in Louisiana accounts for employment of 75,000 more people. All told petrochemicals account for one in four jobs in Louisiana.

In addition, if the production of basic, bulk petrochemicals does shift overseas due to such practices as two tier pricing, does anyone believe that production of specialty petrochemicals will not eventually shift there as well? When U.S. petrochemical facilities close, oil and natural gas suppliers will lose one of their largest customers—raising the prices for oil and natural gas to all remaining customers. Finally, when petrochemicals like fertilizer are produced abroad, we will be open to the same interruptions in supply and the same price manipulations as we have suffered with oil imports. This will jeopardize the interests of both farmers and consumers.

The challenge facing the U.S. petrochemical industry is different from that faced by many industries that come before this Subcommittee. Fortunately the impact of petrochemical imports is only beginning to be felt and the industry is not yet on its knees begging for help. Foreign petrochemicals facilities are just beginning to be built. Initially the energy-rich countries have targetted ammonia, carbon black and a few other bulk petrochemicals, which is why so much of this debate has focused on these commodities. But, in time, as new plants are built one-by-one, other petrochemical producers will awaken to the impact of two tier pricing.

In this legislation we have a rare chance to take action before the damage is done. We have a chance here to ensure that the U.S. petrochemical industry will have a fair opportunity to compete—and to adjust. By providing an adequate remedy for two tier pricing at this time, the Congress can avoid some of the inevitable calls for government assistance that will be heard if the industry loses its competitive edge. Given a fair chance to compete, we can welcome international competition. It will bring benefits to both producers and consumers in this country.

[ATTACHMENT]

PETROCHEMICAL IMPORT LEGISLATION: CHRONOLOGY

October 28, 1982.—Anhydrous ammonia producers petition Commerce Department for countervailing duty to offset subsidy to Mexican ammonia producers.

November 3, 1982.—Carbon black producers petition Commerce Department for countervailing duty to offset subsidy to Mexican carbon black producers.

January 21, 1983.—Gillis Long writes to the Chairman of the International Trade Commission in support of petition by anhydrous ammonia producers for investigation under section 337 of Mexican ammonia imports.

February 24, 1983.—I.T.C. denies petition for section 337 investigation.

March 28, 1983.—Commerce Department issues preliminary determination in anhydrous ammonia case, holding that the two-tier pricing system in Mexico does not confer a subsidy.

April 4, 1983.—Commerce Department issues preliminary determination in carbon black case, same ruling.

May 16, 1983.—Gillis Long writes to Commerce Department asking for explanation on ruling that two-tier pricing system does not confer a subsidy.

June 10, 1983.—Commerce Department issues final determination in anhydrous ammonia case, reaffirming preliminary determination.

June 11, 1983.—Gillis Long announces that he is drafting legislation to reverse the Commerce Department's ruling on two-tier pricing.

June 16, 1983.—Commerce Department issues final determination in carbon black case, reaffirming preliminary determination.

June 28, 1983.—Commerce Department answers Gillis Long Letter on two-tier pricing, explaining basis for ruling.

August 4, 1983.—Gillis Long introduces H.R. 3801, amending the countervailing duty law to provide remedy for two-tier pricing subsidies.

October 20, 1983.—Ways and Means Trade Subcommittee holds hearing on two-tier pricing of energy inputs.

Chairman GIBBONS. Before I go any further I want to say that we are embarked on a serious reform of the countervailing duties and antidumping laws. There is no doubt that what we do in this Congress will not only have impact in this Nation but around the world.

If other people wish to emulate them I encourage them to do so. For one, I am trying to create an atmosphere in which we can have free trade. Subsidized trade is not free trade. It is a perversion of free trade. It has been outlawed by this country for almost 100 years. In the General Agreement on Tariff and Trade we agreed to do away with subsidies. In the Subsidies Code that we entered into in 1979 with all the other trading nations of the world who cared to join we agreed to outlaw subsidies as a distortion of the free trading principle.

Just because we outlaw something doesn't mean it will stop, and those who are innovative will find ways around it. Therefore, this is a part of the continuing process of trying to level the playing field. We don't want to treat anyone unjustly but we cannot have a free and competitive trading system if it is going to have all kinds of artificial distortions in it that upset the marketplace.

This two-tiered pricing system of natural resources is just one of the problems that we face. It is a very vexatious problem, a very sensitive problem. I fear it will become a growing problem unless we find some sensible remedy to it.

So that is the purpose of this hearing today.

Now, would any of my colleagues at the table like to make a statement?

Mr. Schulze.

Mr. SCHULZE. No, thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Moore.

Mr. MOORE. No, thank you, Mr. Chairman.

Chairman GIBBONS. Our first witness is Hon. Alan B. Mollohan. We welcome you here, sir.

STATEMENT OF HON. ALAN B. MOLLOHAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF WEST VIRGINIA

Mr. MOLLOHAN. Thank you, Mr. Chairman.

Mr. Chairman and members of the subcommittee, I appreciate the opportunity to testify before you today on a problem of critical importance to the residents of my district and on the needed remedies to this problem. The problem is unfair foreign trade practices and the remedy is H.R. 3801, a bill to amend the definition of what constitutes a subsidy under our trade laws.

Mr. Chairman, my district, which includes the industrialized northern panhandle of West Virginia, is familiar with this issue. We have faced unfair foreign competition in our pottery, steel, and glass industries. Unfortunately, I have to add yet another industry to this growing list: the chemical industry.

Cabot Corp. is a chemical company that operates a plant in Parkersburg, W. Va. The plant employs 100 people in the production of a substance known as carbon black, which is used primarily as a reinforcing agent in rubber products.

In addition to the multitude of domestic economic problems troubling this—and most of our other—industry today, the people working at this plant are threatened by trading practices of our southern neighbor, Mexico. The Mexican Government controls the country's petroleum industry, including the production of the feedstock used to produce carbon black. The feedstock, by the way, constitutes 70 percent of the final cost of producing carbon black.

Mexican carbon black manufacturers purchase this feedstock for $2 per barrel from their own country. U.S. carbon black manufacturers, however, are unable to purchase the Mexican feedstock at any price. I might add that this is in spite of the fact that such sales could bring Mexico much-needed dollars with which the Mexican Government could repay U.S. bankers some of their enormous debt. Consequently, U.S. manufacturers of carbon black must pay $26 per barrel on the world market.

When the American carbon black producers brought this dramatic price differential to the attention of the Commerce Department in a suit based on Mexican Government subsidies of the feedstock, the Commerce Department determined that no countervailing duty was warranted. The basis for the finding was that our foreign trade laws do not recognize indirect government subsidies made available to entire industries.

Our failure to respond adequately to this problem means American carbon black producers are selling their product on the world market having had to pay, based on my calculations, 1,300 percent more for their primary raw materials than Mexican producers paid. This is foreign trade, but I submit it is neither free nor fair trade.

The impact on our domestic carbon black market of our failure to take remedial action has been dramatic. It was recently announced that one of the Mexican carbon black producers plans to export 228 percent more carbon black into the United States in 1983 than it did last year, and the company expects a continuing increase in its export levels to the United States.

Additionally, a spokesman for one of the two Mexican companies producing carbon black stated that their company was taking advantage of recent carbon black plant closings in countries, including the United States, because of a surplus in the product. I am sure I need not elaborate on the implications of this remark.

Let me simply say that one does not have to adhere to radical protectionist principles to believe our trade laws ought to address and remedy this situation.

I believe the approach set forth in H.R. 3801, a bill I was proud to join Messrs. Long, Whitten, Jones and Hightower in introducing, is a reasonable approach that would address this and other similar situations in the ammonia, cement and petrochemical industries without shutting down our borders to the foreign trade upon which we increasingly depend.

Redefining what constitutes a subsidy to include situations in which the cost of production is artificially depressed by the application of state controls over the price of materials used is reasonable and necessary.

Mr. Chairman, the world of international trade, as you and the other members of the subcommittee are well aware, has changed dramatically over the last few years. We must continue to adapt our trade laws to remain current with these changes. Blinding ourselves to the presence of state-controlled economies and indirect subsidies to industries in these economies will only exacerbate the problem. There can be only one result of our failure to act: Further erosion of our ability to compete fairly in the international marketplace.

Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Mollohan, I agree with the thrust of your statement. We face a world in which there are all kinds of distortions of the marketplace out there. If countries wish to distort their marketplace, that is their own decision, but when it injures our economy is when it becomes our concern.

I think you have put your finger right on the thrust of the problem we have here today. You touched upon the problem with this specific subsidy. With a $2 domestic price versus a $26 export price, the resulting $24 difference has to be the subsidy, even though it is indirectly administered. It is the same kind of problem we face in other areas; another vexatious part of the bill is how we define pricing in a nonmarket economy. Perhaps we will have to go more into that before we find a solution to it.

I want to commend you for your clear and fine thinking and for coming here and helping us solve this riddle.

Mr. MOLLOHAN. Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Schulze.

Mr. SCHULZE. Thank you, Mr. Chairman.

I would like to thank our colleague for his testimony, and for my edification would you tell me a little more about H.R. 3801. I am not familiar with its contents.

Mr. MOLLOHAN. The provision I am specifically interested in relates to the definition of subsidy, and as I have described it in my testimony, the situation which brought it most poignantly to my attention relates to carbon black, and specifically that industry's petition to have the indirect feedstock subsidy that Mexico provides its carbon black industry, countervailable.

It was determined that the fact that the Mexican Government provides the petroleum feedstock which constitutes 70 percent of the manufacturing cost of carbon black, to the Mexican producers for $2 a barrel when the world market price is $26 a barrel, and does not provide that feedstock to any industry other than the Mexican industry, does not constitute a countervailable subsidy, as was claimed in petition before the Department of Commerce.

It was determined that the subsidy was not countervailable because the feedstock was made available to all Mexican industries generally, the theory being under our foreign trade laws that if it is not directed to one industry to benefit one industry it is not preferential treatment. Therefore, it should not be countervailable.

I see that and many other people see this view as a real loophole—a failure in our ability to address what is really an international foreign trade problem that we all should agree needs to be addressed. This is a dramatic example of the failure of our laws to address at least this important aspect of the subsidy problem.

So as I am interested in this section which would redefine the subsidy provision to take into consideration indirect subsidies and to make them countervailable.

Mr. SCHULZE. Are there other provisions or is the redefinition of subsidy the main thrust of H.R. 3801?

Mr. MOLLOHAN. To the extent I am interested in it that is the main thrust.

Mr. SCHULZE. It is not a comprehensive trade bill or anything like that?

Mr. MOLLOHAN. It addresses with the foreign trade problems facing petrochemical industry specifically, as I am familiar with it.

Mr. SCHULZE. I thank the gentleman.

Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Hance.

Mr. HANCE. Thank you very much.

I just wanted to say to my colleague that I appreciate your testimony. One of the things you point out concerning carbon black is what we are facing in many other industries, including cement, and it has had the same devastating effect. We are not playing in the same ball park with the same rules. Hopefully we will be able to address this.

Thank you for your testimony.

Mr. MOLLOHAN. Thank you.

Chairman GIBBONS. Thank you very much.

Mr. MOLLOHAN. Thank you, Mr. Chairman, it is a pleasure to appear before the committee.

Chairman GIBBONS. Mr. Moore, Henson Moore of Louisiana, a member of our committee.

STATEMENT OF HON. W. HENSON MOORE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF LOUISIANA

Mr. MOORE. Thank you, Mr. Chairman.

As a former member of the subcommittee I want to thank the chairman for the opportunity to discuss this.

Chairman GIBBONS. We still think of you as a Member, you can come in and vote any time you can get away with it.

Mr. MOORE. I want to congratulate the chairman and the subcommittee for tackling what has been a difficult problem for a long, long time and hopefully being able to resolve it.

I have introduced a bill, H.R. 4015, which I have spoken to the subcommittee about to establish a special rule for the treatment under the law of natural resources and their byproducts.

Currently there are some governments through regulation are setting the price artificially low of a natural resource used as a raw material such as natural gas in production of their export materials such as chemicals. That preferential rate is available to manufacturers within their own country but that same price is not available to purchasers outside their country.

As a result these foreign manufacturers are granted an unfair competitive advantage when they later export the finished product to the United States at a subsidized price because of their access to artificially inexpensive natural gas.

The bill I have introduced would determine the level of subsidy by taking the difference between the regulated price in that home market in the foreign country and the fair market value of the natural resource that would occur without government regulation in that country.

The fair market value is determined or imputed by several criteria, including the world price of the natural resource or byproduct, the average price generally available to the U.S. producers, cost of production, the condition of the market, and the existence of dual pricing. It has become clear to the members of this subcommittee that preferential treatment of certain natural resources does in fact exist and in fact that revelation is the reason we are here today to discuss the several measures being offered to the subcommittee as a way to work our way out of that morass.

The advantage to my approach in H.R. 4015 is twofold, first it allows the principles of free trade to be continued and second, it provides internationally defensible benchmarks against which any regulated price can be compared. This subcommittee has considered other approaches including using simply the export price as the measure or the combination of the export price or the price generally available to U.S. producers.

Mr. Chairman, none of the three approaches you have before you, these two or the one I am suggesting, are perfect. They have all got problems. The subcommittee has to work with all of them and try to make one of them work.

The one I have offered tries to impute what the market price is in a country. That imputation is imperfect by itself, you are creating something that doesn't exist.

However, as imperfect as that is it offers the subcommittee a vehicle to work on and try to make something work. We have obvious problems with the other two approaches. Using simply the export price if the export price was in fact a realistic market price all over the world, there would be no problems. But we know in several countries, Canada and Mexico, for instance, their export price is an artificially high price to discourage, I assume, export of that particular raw material.

Therefore, to latch on that figure and say that is the benchmark, I think will cause us great difficulties with GATT, great difficulties with the trading partners because it is an artificially high price.

A number of people who are supporting what has to be done or doing something about upstream subsidy of raw material agree that the export price really cannot be used.

The third one being considered is the export price or the price available generally to U.S. producers. I have mentioned the problems with the export price. The problem with the price available to U.S. producers is the fact I think it violates GATT because you set up as a world standard for countervailing duty what a U.S. producer can get something for. That does not consider the comparative advantage that a foreign country may have by oversupply of gas and underutilization of gas, a country such as Saudi Arabia or many others.

Therefore we are getting into trouble if we adopt a standard such as that.

I think it is very important that whatever action is taken by the subcommittee, not only be fair and preserve free trade, but if it is going to be just protective and not going to be fair, then we have got to realize that every other country in the world will mirror what we have done and take the same action and we may wind up being the net loser by the action we take today.

In 1982 alone the U.S. chemical industry exported over $12.8 billion worth of products. We don't want to interfere with that export. At the same time we do need to address this problem of subsidization of upstream raw materials.

Mexico, for instance, is our third largest trading partner. It is to our advantage to work out and abide by an acceptable trade principle because we realize that Pemex is one of the worst offenders in Mexico now, the upstream subsidy of natural gas. But to adopt a standard we cannot live by would mean we would lose perhaps Mexico as a trading partner.

It is important that we establish a long-term policy that is fair to all U.S. producers that is predictable and reasonable.

We think that H.R. 4015 will do this by instructing the Commerce Department to change its policy of the general availability test to a more comprehensive test taking into account the world price, generally available price, cost of production, market depreciation, and dual pricing. All of these points are important and we can live with that standard when it is mirrored by foreign countries against any foreign export that we export into those countries.

The petrochemical industry in Louisiana is a good example, we have more than 31,000 people in my State that are directly involved in manufacturing of petrochemicals, nationally I am told over 900,000 people in this country are involved with it. Products being manufactured in this country are in excess of $170 billion in value. When we look at the International Trade Commission's April 1983 report we can see that developing nations such as Saudi Arabia, Indonesia, Kuwait, Canada, Soviet Union, People's Republic of China, will place increasing importance on development and growth of their own petrochemical industries and will be devoting government resources to this expansion.

Because of this rapid development, because of this expansion, many questions arise but the most obvious result is a reduced U.S. share of the total export market and in some cases the United

States may become a net importer of chemicals where we were once an exporter.

In 1980 for example, we claimed 45 percent of the world exports for ethylene, according to the ITC, by 1990, we will be a net importer of ethylene.

Every major chemical, ammonia, methanol, many others, the U.S. percentage of world capacity will decline as the other countries begin to develop their resources and gain control.

We are no longer going to enjoy the leadership in this area. Not only will we not be the leaders but we may be faced with impacts of reductions in amount of chemicals and value we produce of $170 billion down. The reduction in jobs of nearly 1 million is possible. If the United States will remain competitive in this market the unfair advantage of foreign subsidization must be offset with a reasonable countervailing duty which reflects the real subsidization and doesn't become an overly protective measure we cannot live with when other countries adopt a similar position.

There is a delicate balance which must be achieved in determining the level of subsidization. It is for this reason that I have offered H.R. 4015 for consideration of this subcommittee as an alternative to what the subcommittee is currently addressing.

Chairman GIBBONS. Mr. Moore, it is because of my respect for your wisdom and my respect for your ability that we paused to have these hearings today. Let's take Mr. Mollohan's example just to work with, get out your paper and pencil there.

He said that $2 was the price per barrel of oil in Mexico and the export price was $26 a barrel, and that because of this differential his carbon black industry was seriously injured.

So he figured there was a $24 subsidy there.

Now, what would the subsidy amount to with those same facts under your proposal?

Mr. MOORE. Mr. Chairman, I think it would be the same figure. The H.R. 4015 bill I have offered doesn't say you use simply one, you use a combination to arrive at what the domestic market price is for that raw material in Mexico. I think it would come out with probably the same figure, $26 a barrel or somewhere in that area, meaning you have the subsidy of $24 a barrel and a countervailing duty in that amount.

I might say that Mr. Mollohan's problem of carbon black exists in my State and we are in competition with Pemex plants in Mexico.

Chairman GIBBONS. How does your proposal differ from measuring it at the border. They set the price.

Mr. MOORE. The difference is this and it is important: You offer the Department of Commerce the flexibility to be sure it is not accepting an artificial price and the export price can in fact be an artificial price. It is in natural gas coming from Mexico, not necessarily perhaps in oil.

You are offering the Department of Commerce a range of factors to look at to try to find what the price is. In oil it seems to be simpler. There is a recognized world price for oil, a recognized export price for oil, and I think that because it can be traded back and forth between our borders so easily you could come to a quick conclusion of what the price of oil is.

Chairman GIBBONS. We have disposed of oil, we know that now. How about natural gas? That is another serious problem. Natural gas is not transmitted across oceans very well but it is transmitted across borders pretty easily.

I cannot give you the exact price of natural gas at the border. I think it is about $4 or something like that—I don't want to speculate what it is because I don't actually know.

How would it figure in natural gas? What would be the different factors? Both come out of the same hole in the ground almost, and go through a little different processing, the transportation is a little different.

Mr. MOORE. Mr. Chairman, staff advised me they think the export price of natural gas out of Canada and Mexico is the same figure, about $4.40 a thousand cubic feet.

Chairman GIBBONS. Something like that, yes.

Mr. MOORE. That is believed to be an artificial price, higher than the free market price would be.

The free market price is lower. Probably closer to what American producers pay for natural gas, somewhere around $3 or $3.50 a thousand cubic feet. It would be easier to determine with countries on our borders than it would be a country like Saudi Arabia. What is the domestic price of natural gas in Saudi Arabia? That is a difficult question to ascertain. That is why you have to have a range of ways of doing it, such as H.R. 4015 offers rather than pegging it to one or two simple things that may turn out to be very, very unfair.

Chairman GIBBONS. One reason for setting it at the border was that people could control what they do within their own borders and they have every right to do. It is only when that product enters the stream of international commerce and only when it injuriously affects our own industry that we take any action under this legislation.

Let's go back to oil, either the $2 a barrel Mexican price is artificial or the $26 a barrel is artificial, and that is up to them to decide which is artificial.

They could ignore us if they want to and we will have to take whatever action we can in this country after they decide whatever price they want to accept.

I have a hard time figuring out where you differ so greatly from our border pricing solution. The country involved fixes the border price. The country involved fixes the artificial internal price. It seems we should let sovereign countries alone and let them do what they want to in their own countries.

But when it comes across the border and seriously affects us is when we should worry about it. That is what we were aiming at in having a simple direct test rather than one full of discretionary provisions. Maybe we do need a discretionary one but I have not yet been convinced of that.

Do you have anything you would like to add?

Mr. MOORE. Mr. Chairman, the export price is certainly a far simpler way to go about it. That has great attraction, for me. It also offers greater protection for our industries which is also something that we would like to do if we can get away with it without interfering with foreign trade.

Chairman GIBBONS. It is not a violation of GATT.

Mr. MOORE. It may be an artificial price that has to do with exchange currencies. It may be because the country decided it doesn't want to sell something overseas, so it prices it artificially high.

Chairman GIBBONS. There would not be a price at the border then if they didn't want to export it. There would be no actionable problem if they didn't want to sell overseas.

Mr. MOORE. In fact, that could be the case. So they put a high price. They want to retain it to attract industries to come in and use it. Industries came into Kent Hance's State and mine because of cheap natural gas once upon a time—it was 15, 17 cents a thousand cubic feet—and that is why they came to Louisiana, and we were not anxious to sell——

Chairman GIBBONS. You are part of the United States; at least Texas was, last time I checked.

Mr. HANCE. Still is.

Chairman GIBBONS. We are talking about international trade now.

Mr. MOORE. We had a Governor in Louisiana abrogate the interstate contracts, to keep it in our State.

Chairman GIBBONS. You didn't get away with it.

Mr. MOORE. That is right. But the point is that the foreign country wouldn't be determining what the fair price would be under H.R. 4015. It would be the Commerce Department. We are giving them a range to see if the export price is a fair price as it is in oil. That is the way it is. If it is an artificial price, look at other factors to determine the fair price.

Natural gas in Canada and Mexico would not be difficult to ascertain. It would be close to the market price in the United States.

Chairman GIBBONS. One of the reasons I want this definite is I am not satisfied with the Commerce situation. I am here trying to change the law. I think they should have found those to be actionable subsidizes on those cases that we heard about today. They just didn't have the guts to do it. I will hear from them in a few minutes. I am here to change that law.

You know, for years we couldn't get Treasury to do a cottonpicking thing about countervailing duties. They sat on the cases so long that the roaches ate the papers down there. We finally transferred authority over to Commerce. Commerce does a little better, but they like that discretion, you know, and they go around pontificating about what the law is. I want to set it down clear so they will understand what the law is, and everybody elsewhere will.

You are a lawyer and I am a lawyer, and I like to see it black and white about what the law is. I don't have a problem advising my client about the law when it is spelled out. That is what I am trying to do here.

Mr. MOORE. Let me say I am no defender of the past actions of the Commerce Department, but there has been a big change. No matter what this subcommittee passes, you will go from a general availability test to something else. H.R. 4015 does that, too. You are forcing them away from that and into a new ball game.

Even in the case of oil, Mr. Chairman, no matter how clear the law is on the books, we wind up going to court to resolve the interpretation of the law. That is what I am worried about.

If we take just a simple—what looks simple to us as lawmakers—test, we may wind up in a lot of courts somewhere along the line to resolve it. Look at the United States. You can't take any one price here to determine the domestic price of gas. It ranges from 20 cents a thousand to $7 or $8 or $9 a thousand feet, depending on the contract you sign.

You have to look at the whole market and take a rolling average and come out with what we think to be a fair domestic price for natural gas in this country, which isn't fair to two different companies in the country, one with old contracts, one with new contracts, which are more expensive.

It is just not simple. You have to give the Commerce Department a range to look at to be sure we don't wind up in trying to preserve free trade—as this chairman and this subcommittee championed for so many years—that we don't wind up doing something else we will have to undo or that the administration won't sign or that will end up hurting our industries by doing something so simple that it may well wind up being problematical.

Chairman GIBBONS. Mr. Hance.

Mr. HANCE. Thank you, Mr. Chairman.

Mr. Moore, I appreciate your testimony. I appreciate your efforts in helping to develop criteria to measure the actual amount of the subsidies we are discussing.

One of the things we are talking about is the complications associated with your approach. What I propose and what Mr. Gibbons proposes, on the other hand, might be too simple. I think back, however, to the law professor I had who said that it is not important that you make a law where people can understand it; it is important that you make it so clear that they can't misunderstand it.

That is what I want to do, because I have dealt with the Commerce Department. We have been dealing with them on this subcommittee with the issue of oil company tubular goods. Last month the Europeans went way over their agreed to limits for the entire year; yet they have another 6 months to go in the year. The Commerce Department keeps saying that they are going to look into the problem. But they don't do anything.

So I think the problem is that the approach you are talking about is complicated and will result in giving the Commerce Department too much discretion. I know you want to give them discretion, but I just don't feel that with the changes made over there from administration to administration that we should be giving the Department that much discretion. To pass a bill that would be ineffective by individuals who disagree with it would just complicate and frustrate the matter.

One thing I want to ask you is whether the intent of your proposal is to allow Commerce to determine the value of this energy subsidy at a level that is below the cost that the product could be freely purchased on the world market?

Mr. MOORE. Would you ask that again, Mr. Hance?

Mr. HANCE. Is it the intent of your bill to allow Commerce to determine the value of the subsidy at a level that would be below the price that the product could be purchased on the world market for?

Mr. MOORE. That could happen, but that is not what H.R. 4015 says. It says one of the things they consider is the world price.

Mr. HANCE. That is what gives me a lot of concern. You know, I think that it could have that effect, and if it gives them an easy out. I think it is obvious that it could——

Mr. MOORE. I didn't say it gives them an out. You just never know what a court will do. That could happen. Human beings could interpret it differently.

One of the things we are writing in—and it could be tightened up if the subcommittee saw fit—is one of the things you look at in computing the domestic price is what the world price of the product is? In natural gas, you have a hard time determining world price. You don't for oil; you don't for bauxite.

Mr. HANCE. I think that your proposal would allow the Commerce Department to come back and say, "We think the subsidy is below the cost that the product could be freely purchased on the world market." If it did, I don't disagree with you on what the courts would do. I think that is to be determined by a court.

But my concern is that the court looks at the intent of the legislation and tries to carry out the legislation considering the intent and the wording; whereas, many times in the Commerce Department you may have somebody that just disagrees with the legislation and they are going to carry it out however they see fit. We have to ride herd on them.

I think there are some industries that probably can't continue to keep their heads above water while we go through the legislative process. Then we come back and have to ride herd on Commerce. That is what concerns me, really.

Mr. MOORE. I thoroughly agree with the gentleman. We have that problem with every law we pass in the Congress of the United States.

One of the problems is, in some cases, even if we pass an export price test, when Saudi Arabia comes onstream, it is worth 10 cents a thousand foot. They are delaying it. They don't have a use. This won't help. The test here won't help. They will be able to undercut every bulk commodity manufacturer in this country.

I don't think we can look to the Commerce Department or this statute taking away the comparative advantage that a foreign country is going to have. All we can do is try to prevent unfair competitive advantages from occurring and then let the chips fall where they may as to the future of the chemical industry in this country, which is already in a state of change from bulk to specialty chemicals, because of just what we are talking about. They see potential competition with Saudi Arabia that is impossible to meet.

Mr. HANCE. Under your proposal, if you were asked what the true value of crude oil is, what would you say from your legislation?

Mr. MOORE. Under this legislation, that would not be difficult to compute. There is a world price; there is an export price of oil that seems close to that in the case of Mexico. So I think you would wind up with a figure very close to what Mr. Mollohan suggested under his bill, because the price of oil is a fairly easy one to determine. Natural gas is more difficult.

Mr. HANCE. One question Mr. Gibbons has already asked but that is important: What price for crude oil do you think your approach would measure?

Mr. MOORE. The same as Mr. Mollohan's. His price was $26 for the export price for oil. Pemex is selling it to their companies at $2 a barrel, so the price would be $24, the countervailing duty, under his bill or my approach.

Mr. HANCE. There is nothing in your approach that would prevent Commerce from coming out with a lower price.

Mr. MOORE. They could look at other things, right. You can certainly challenge their decision if they came up with something lower.

Let me give another example of what is wrong with the export price approach. What do you do in a situation where Saudi Arabia—they can't export natural gas; it is too expensive to liquefy—assume they set an export price of 10 cents per thousand, but you can't get it. Then they sell it to their companies at 50 cents per cubic foot, so there is no export price test; there is no subsidy.

What about Mexico that gets around it by saying, "We will set a quota; we will set the price of natural gas at $2.50 or $2 per thousand cubic feet." Whatever the same price is, they are giving it to their chemical prices, but they put a quota on and say they will only sell a million cubic feet, first come, first served.

Chairman GIBBONS. Can I interrupt?

Maybe one of the things we ought to do is adopt your test where there is no export price.

Mr. MOORE. That is a possibility.

Chairman GIBBONS. In Saudi Arabia, we could adopt a fair market price test there because there are no exports. But in a border area where there are exports, we could adopt the export price.

What is wrong with that?

Mr. MOORE. That is what I propose in H.R. 4015. You give the Commerce Department the flexibility to do just that.

Chairman GIBBONS. That is not how I understand H.R. 4015. You would apply the same price in that bill, this estimate that Commerce is going to make, even where there is an export price.

What I am saying is where there is export price, you use that; where there is not an export price, we use the fair market price.

Mr. MOORE. Mr. Chairman, that——

Chairman GIBBONS. Either/or. You maybe opened up some of the——

Mr. MOORE. I think what you are saying is what I am suggesting, Mr. Chairman. You think about a flexible standard you can use, because I don't think there is going to be one you can live with worldwide. But even with the chairman's suggestion, you have to find a way to get around a quota situation where Mexico says, all right, we will play that game; we will set a low export price that meets the price for our companies, but then set the quota. You are right back where you started from.

If you had just one way of getting at that imputed market price in that country, you end up in that situation.

Chairman GIBBONS. Thank you.

Mr. HANCE. There is not an export price for natural gas in Saudi Arabia. If they set it at 10 cents, that would not be an export price, because you can't get it at that price.

Mr. MOORE. But they would tell you, Mr. Hance, "We would be glad to sell it to you at that price; come and get it."

Mr. HANCE. Are you going to take a sack over there and get it? They have no delivery system.

Mr. MOORE. But if you have just an export price test, that is one of the problems you get into. You have to come back and get around that.

Mr. HANCE. I think we can clarify that for the record by saying that the export price would have to be a deliverable price, something they could deliver.

Mr. MOORE. What would you do with Saudi Arabia under the export price test?

Mr. HANCE. If they could deliver?

Mr. MOORE. What happens if they say, "We can't deliver it, so we don't have a price"?

Mr. HANCE. So they don't have one.

Mr. MOORE. How do you measure if there is any subsidization going on under the export test?

Mr. HANCE. You test it against the world market price.

Mr. MOORE. That is not fair to Saudi Arabia if they sell it and they can't—in fact, they are not perhaps subsidizing it at all. You are imputing a subsidy to them which is really unfair to them.

Mr. HANCE. That is not one of my concerns, whether it is fair to Saudi Arabia or not. They don't have a whole lot of popular activity in my district.

Mr. MOORE. I fully agree with you. Votewise you are entirely right.

That is not how free trade works. Free trade works where you have to give the country the fair competitive advantage they have; otherwise, we won't export to anybody if they mirror the same thing on us.

Mr. HANCE. I agree with you. You have got to be fair. But I tell you, I think the American public is beginning to see that we have just been chumps on a lot of these things and that there are many, many countries that are taking complete unfair advantage of us. They have for many years.

One other question I wanted to ask you. During our committee discussions, some of the members of the committee argued that if the natural resource was sold for 1 cent above its production cost, that it would not be a subsidy.

Would you agree or disagree with that?

Mr. MOORE. I disagree with that. I certainly disagree with that. I think H.R. 4015 tries to find what the real market price is.

Mr. HANCE. OK.

Mr. MOORE. We send a lot of grain. It comes out of your State and mine and out of the Midwest. If we start putting a test on, like you described, for Saudi Arabia, they might not buy from us and other countries may not buy from us, and this has a ramification that goes a lot further than just the chemical industries.

I am trying to point out, whatever we pass—and we have to pass something, we all agree on that—we are trying to get the problem of these upstream subsidies, but whatever we pass has to be something we can live with in the totality of the trade world and in our own products exported from this country.

Mr. HANCE. You are not saying the grain price would be unavailable. With grain, however, it is not like Saudi Arabia not being able to deliver gas.

Mr. MOORE. But they will come back and say: "What you have done to us is put the blocks to us, given us"—"You imputed to us a subsidy that doesn't really exist, and you are penalizing us. So, therefore we will just take trade retribution action against you."

Mr. HANCE. Of course, I am one that thinks that at some point in time we may have to have some type of overall legislation that would say that you would come back and have a percentage tariff on the goods of a country, determined by the percentage they put on us.

Mr. MOORE. That goes to the foreign field, and I am not here to talk about that this morning. But I am hoping, No. 1, we have to address upstream subsidies; and No. 2, we are trying to do it and determine what is the subsidy.

You start dealing with the Soviet Union or any state-controlled economy, it is very difficult. When you do it even in Mexico and Canada, it is less difficult but still a problem to us.

All I am suggesting is that I have not seen yet—and I have every chemical company that exists anywhere else in the country in my State—I am very, very concerned that we don't do something that we can't live with when the rest of the countries begin to adopt it, or somewhere along the line the President of the United States says: "That is unfair, I have been advised by my State Department, that seems to monkey with all the trade problems, and the STR says it is unfair," and he vetoes it, and we are back to square one.

I am hoping we come up with something that is not perhaps as simple as we would like to see but that is fair to make free trade a real possibility.

Mr. HANCE. You mentioned we are losing a lot of the petrochemical market. I think that is because our competitors overseas are subsidizing their products in one form or another and it is extremely difficult for us to compete under those circumstances.

Mr. MOORE. Our chemical exports are still continuing to go up. We hope it will continue.

Mr. Hance, let me say I don't think you can say that every single market we lose is due to unfair subsidization.

Mr. HANCE. I agree with you.

Mr. MOORE. There are countries like Saudi Arabia that will flat be able to meet us on raw material prices. Therefore, you can't concoct a system that protects us, because that is protectionism; not free trade.

Mr. HANCE. Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Frenzel.

Mr. FRENZEL. I want to thank the witness. I am sorry I was not here for the beginning of his presentation.

When the committee began to discuss this bill in subcommittee, the gentleman from Louisiana made I think a real contribution by pointing out some of the difficulties with the material that we were working with. You now believe that H.R. 4015, your bill, if substituted for your original amendment, will give us a workable—is that the number of your bill——

Chairman GIBBONS. Yes.

Mr. FRENZEL [continuing]. Will give us a workable upstream subsidies section?

Mr. MOORE. When I was an interloper allowed by the graciousness of the subcommittee chairman to speak at that markup, I proposed the same thing as we have in H.R. 4015. I suggest this would be more workable. It is less certain, less simple; but it is more workable.

I would also suggest that what we have put together with the staff of this subcommittee is by no means the perfect answer and that the subcommittee should feel free to address any of these suggested tests and refine them or close loopholes you point out or whatever.

But what I tried to say in the beginning is the fact that the subcommittee is faced with several choices—the export test, the export or material available to U.S. producer test, or what we offer, which we think runs into far less problems with GATT, less problems with charges of protectionism and at the same time tries to get at what is the market price of a subsidized raw material.

Mr. FRENZEL. If I understand your discussions with Mr. Hance, your allegation is that any provision which does not at least take into account the cost of production is going to leave us vulnerable to retaliation?

Mr. MOORE. I think that is correct.

Mr. FRENZEL. We have only seen the tip of this iceberg. We have been talking about petrochemicals mostly. I am sure we will hear about other resources and other products as we go on.

At the moment, I am inclined to agree with you that this briarpatch has more thorns in it than we originally suspected, and that this is perhaps the very least that we can do to make sure it won't put us in any trouble as regards protectionism.

I thank the gentleman. We need your help.

Mr. MOORE. I thank the gentleman.

If I could impose on the subcommittee's time, let me say the chemical exports are going up. We changed into specialties. We don't want to do anything here that interferes with export of those specialty chemicals.

Second, we have a lot of chemical companies—and Mr. Hance and I are familiar with them—that while we have some that would love a tough protectionism measure such as an export test, we have others that are very much opposed, because they are located offshore and have offshore subsidiaries taking advantage of those. We will have those folks going to the White House asking for a veto on grounds of fairness, because it is their own profits on the line through foreign subsidiaries.

What we are saying is we don't have all the chemical companies behind us in doing something here. That is why as a practical matter we have to do something that is practical and evenly balanced.

I thank the committee for hearing me out on this issue.

Chairman GIBBONS. Mr. Moore, I have one more colloquy I want to carry on with you. I have been sitting here writing as you have been talking, and as other members have been asking questions, and I am trying to improve this.

As you know, all three alternatives we have here require the finding that the controlled resource constitutes a significant portion of the resulting product's manufactured cost. That is common to all the proposals we have.

Mr. MOORE. Yes.

Chairman GIBBONS. In other words, there must be findings that the resource controls a significant portion of the resulting product's manufactured cost and that the export of the resultant products are causing material injury to the U.S. producers of a like product.

Now, first we would come in with a border test. Then we went to what we called option two, which is a border test with an upset provision if the U.S. domestic price is lower than that anyway, or even with that.

Now, with all those caveats in there, I would say it is the export price with all the caveats, or where there is no export price available; or where export quotas have distorted the export price, then a fair market price, a computed price. That, I think, gives certainty where there is a clear export price and takes into consideration many of the other factors—I am not sure all of them.

I throw it out for you to think about. Maybe you don't want to answer now. Maybe we can hash it over in the next few days, where the export quotas or levies that distort the export price; then a fair market price.

Mr. MOORE. Mr. Chairman, I think you are getting there, and I can't answer it right now. I want to think that through. I think you are showing the need for flexibility. And I think that while at the same time trying to make the test I propose simpler. So you are moving toward what we have to do; yes.

Chairman GIBBONS. All I am trying to do is get the playing field level.

Mr. MOORE. That has been your history in free trade, Mr. Chairman.

Mr. HANCE. Mr. Chairman, I have one other question.

When we were talking about the cost of production a while ago, Mr. Moore, there was an indication that is not directly related to the natural resource.

Would you object to dropping that provision in your approach—the cost of production provision?

Mr. MOORE. Let's see about that.

Mr. HANCE. You said it did not relate directly to the value of most natural resources. That is one thing we might consider.

Mr. MOORE. That is one thing; yes.

Mr. HANCE. Thank you very much.

Chairman GIBBONS. Thank you.

We have one of those nuisance votes on over there. Do Members want to go make it or not?

We are going to have to go over. We will be right back. Sorry to keep you waiting, but some fools thought we got to approve the Journal. So we are going to go over there and do it.

[Recess.]

Chairman GIBBONS. The subcommittee will be in order.

I want everybody in the room to know the vigor of that gavel had nothing to do with this room. It is something that is happening in another part of this Congress that I have my attention focused on, too.

Next we have a panel: The U.S. Trade Representative, Mr. Gingrich, and the Department of Commerce, Mr. Holmer.

Mr. Gingrich, you are first.

Mr. GINGRICH. Mr. Holmer will make the Administration statement.

Chairman GIBBONS. Mr. Holmer. OK.

STATEMENT OF ALAN F. HOLMER, DEPUTY ASSISTANT SECRETARY FOR IMPORT ADMINISTRATION, ACCOMPANIED BY JUDITH BELLO, DEPUTY TO THE DEPUTY ASSISTANT SECRETARY FOR POLICY, DEPARTMENT OF COMMERCE; AND CLAUD GINGRICH, GENERAL COUNSEL, U.S. TRADE REPRESENTATIVE

Mr. HOLMER. Mr. Chairman, good morning. I am pleased to appear before you today to describe the countervailing duty decisions by the Department of Commerce which have contributed to congressional interest in the subject of upstream subsidies.

I am accompanied by Mr. Gingrich, as you know, the General Counsel of the USTR, and by my Deputy for Policy, Judy Bello.

I have been asked to recount the principal bases under current law for our negative final determinations on ammonia from Mexico and on softwood lumber products from Canada, and on suggestions for dealing with this area.

The concept of subsidies is used to offset the unfairness created when the Government intervenes and distorts natural comparative advantages or efficiencies. Subsidies are of two types: export and domestic. Export subsidies are those which are given contingent upon export performance or which stimulate export over domestic sales.

They are considered internationally to be bad per se because they are aimed at another country's economy. Domestic subsidies, on the other hand, are expressly recognized by the GATT Subsidies Code as important instruments for the promotion of social and economic policy objectives. They are not considered to be bad per se.

Under current U.S. law, domestic subsidies are potentially countervailable only if provided to a specific enterprise or industry, or group of enterprises or industries.

Chairman GIBBONS. That is the law we are trying to change in this hearing right now.

Mr. HOLMER. That is right. That is the law that is really the subject of this hearing.

Chairman GIBBONS. That is right.

Mr. HOLMER. In other words, a countervailable domestic subsidy is Government action or direction that attempts to give one or more industries a special advantage over other industries in the same economy. But Government programs and activities which are generally available—such as high quality transportation systems, investment tax credits, capital cost recovery allowances, irrigation projects, police and fire protection, rural electrification programs, and public health programs, just to name a few—are not considered to be countervailable domestic subsidies, even though such activities could be said to benefit companies by indirectly lowering cost of production.

That, in a nutshell, is the general philosophy behind our current countervailing duty statute. I would like to review briefly the application of those principles to the decisions in ammonia from Mexico and softwood lumber from Canada.

In their countervailing duty petition, U.S. ammonia producers complained chiefly that Pemex, the Mexican Government-owned entity which monopolizes both natural gas and ammonia production, obtains natural gas much more cheaply than they can. Natural gas accounts for over 85 percent of ammonia's value, so the resulting advantage for Pemex is obviously significant.

Specifically, petitioners charged that Pemex, the Mexican Government-owned and controlled natural gas producer, transfers natural gas to its ammonia production facilities at an internal cost accounting price below the price charged to purchasers of natural gas within Mexico. Our examination of Pemex records proved that the internal transfer price is higher than the price generally available to other industries within Mexico.

The heart of the allegation and the part of it that is really the subject of this hearing is that Pemex sells gas at a price well below a commercially reasonable rate—whether that be the U.S. export price, a price within the U.S. market, an alleged world price, or some other surrogate benchmark such as an opportunity cost. Yet, as I have already explained, Pemex as ammonia producer pays more for gas than the price charged to other industrial users. In other words, the price Pemex pays exceeds the generally available price within Mexico.

Consequently, natural gas is neither provided for ammonia production at preferential rates, nor at a rate cheaper for a "specific * * * industry, or group of * * * industries." The allegedly commercially unreasonable price for gas also does not give rise to an export subsidy.

For all these reasons, Mr. Chairman, the Department concluded that Mexico has not provided countervailable benefits through a selectively available upstream subsidy to its ammonia industry through natural gas pricing and tax policies.

Let me turn now to our CVD investigations of softwood lumber products from Canada. On May 24, the Department issued final determinations that such products receive only de minimis subsidies—less than 0.5 percent ad valorem—so the cases were terminated.

The main allegation—accounting for over 95 percent of all subsidies alleged—was that the Canadian Federal and Provincial Governments give the Canadian forest products industry a domestic subsidy through their stumpage programs. Stumpage programs are the systems by which individuals and companies acquire rights to cut and remove standing timber from Government forest lands. We decided that stumpage programs do not confer a countervailable domestic subsidy, principally for the following reasons.

First, stumpage programs are not provided only to a "specific * * * industry, or group of * * * industries" within Canada. Rather, they are available within Canada on similar terms regardless of the industry or enterprise of the recipient. The only limitations as to the types of industries that use stumpage reflect the inherent characteristics of this natural resource and the current level of technology.

Nominal general availability of a program does not necessarily suffice to avoid its being considered a possible domestic subsidy. The Department further determined that stumpage is used within Canada by several groups of industries. In this regard, we noted that under the classification systems of both Canada and the United States, the lumber and wood products industries, the pulp and paper industries, and the furniture manufacturing industries constitute at least three groups of industries.

Chairman GIBBONS. Is stumpage available to some American concern that would go up there and cut?

Mr. HOLMER. Yes, it is.

In summary, with respect to the Canadian softwood lumber case, we found there were no countervailable benefits. There were no benefits to a specific group of industries and no domestic subsidy since the Government did not provide stumpage at preferential rates; nor did it assume a cost of production.

It should come as no surprise to you, Mr. Chairman, that we believe that the Department of Commerce properly decided the Canadian softwood and Mexican ammonia cases under current law. More importantly, for the purposes of this hearing, we believe that the results reached in those decisions are appropriate and should not be reversed by the amendments proposed, for the following reasons.

First, as reviewed earlier, domestic subsidies are potentially countervailable if provided to a group of enterprises or industries or a specific enterprise. Generally available subsidies, domestic subsidies, do not distort allocation of resources within an economy. Absent any distortion in resource allocation, these merely assist the economy and not particular industries or sector.

Second—and this is an issue that Congressman Moore addressed in his statement, and also Mr. Frenzel did in his exchange with Mr. Moore—we must remember that any precedent we set will likely be emulated by our trading partners. Since U.S. natural gas prices are still regulated, U.S. products such as textiles and petrochemicals which are made using natural gas would be targets for retaliation and CVD petitions abroad. And it is by no means guaranteed that our trading partners would be as careful in their drafting as the subcommittee is attempting to be.

Third, eliminating or qualifying the requirement that a domestic subsidy be provided to a "specific group of * * * industries" would mean that in most cases we would brand as unfair foreign government practices which do not distort resource allocations either within its own economy or vis-a-vis other economies. We would be asked to sit in judgment on the fairness of our trading partners' practices; the unfairness label would itself be perceived by our trading partners as an unfair intrusion into their sovereign and internal policies and practices.

Fourth, we do not think it is fair to preclude other countries with an abundance of natural resources from capitalizing on the comparative advantages of such resources for their economic development. The proposal before the subcommittee would force such natural resources to be sold at prices established by less competitive producers.

Fifth, the proposed amendments would depart significantly from the international consensus on what constitutes a subsidy. It is inconsistent with U.S. obligations under the General Agreement on Tariffs and Trade. The United States is already the most aggressive enforcer and interpreter of the Subsidies Code and of domestic CVD laws. We believe that further distancing the United States ahead of its trading partners in this regard is not in our overall best interest in seeking greater discipline on the use of subsidies.

Mr. Chairman, while we have concerns with respect to the amendments which have been suggested, we look forward to continuing to work closely with you in addressing this issue.

We would be happy to respond to your questions.

[The prepared statement follows:]

Statement of Alan F. Holmer, Deputy Assistant Secretary for Import Administration, Department of Commerce

Mr. Chairman, I am pleased to appear before you today to describe countervailing duty decisions by the Department of Commerce which have contributed to congressional interest in the subject of upstream subsidies. I have been asked to recount the principal bases under current law for our negative final determinations on ammonia from Mexico and on softwood lumber products from Canada.

I. BACKGROUND ON SUBSIDIES

The concept of subsidies is used to offset the unfairness created when the government intervenes and distorts natural comparative advantages or efficiencies. Subsidies are of two types: export and domestic. Export subsidies are those which are given contingent upon export performance or which stimulate export over domestic sales.

They are considered "bad" per se because they are aimed at another country's economy. Domestic subsidies, on the other hand, are expressly recognized by the GATT Subsidies Code as "important instruments for the promotion of social and economic policy objectives." They are not considered bad per se.

Under current U.S. law, domestic subsidies are potentially countervailable only if provided to a "specific enterprise or industry, or group of enterprises or industries." In other words, a countervailable domestic subsidy is government action or direction that attempts to give one or more industries a special advantage over other industries in the same economy. But government programs and activities which are generally available—such as high quality transportation systems, investment tax credits, capital cost recovery allowances, irrigation projects, police and fire protection, rural electrification programs, and public health programs—are not considered to be countervailable domestic subsidies, even though such activities could be said to benefit companies by indirectly lowering cost of production.

That is the general philosophy behind our current countervailing duty statute. I would now like to review the application of those principles to the Mexican ammonia and Canadian lumber cases.

II. AMMONIA FROM MEXICO

In their countervailing duty petition, U.S. ammonia producers complained chiefly that Pemex, the Mexican government-owned entity which monopolizes both natural gas and ammonia production, obtains natural gas much more cheaply than they can. Natural gas accounts for over 85 percent of ammonia's value, so the resulting advantage for Pemex is obviously significant.

Specifically, petitioners charged that Pemex, the Mexican government owned and controlled natural gas producer, transfers natural gas to its ammonia production facilities at an internal cost accounting price below the price charged to purchasers of natural gas within Mexico. To the contrary, our examination of Pemex records proved that the internal transfer price is higher than the price generally available to other industries within Mexico.

Petitioners also alleged that industrial users of natural gas paid a lower price for gas than other users. Although cheaper than the price for residential users in Mexico, the standard industrial price does not benefit a specific industry or group of industries. Under section 771(5)(B) of the Act, therefore, it is not a countervailable domestic subsidy. Nor is the industrial-residential price differential an export subsidy: availability of the lesser price is not contingent upon export performance, and we have no reason to believe that it operates to stimulate export over domestic sales. (Indeed, different rate structures for residential and industrial users are common in the U.S.)

Petitioner's most important allegation is that Pemex sells gas at a price well below a commercially reasonable rate (whether that be the U.S. export price, a price within the U.S. market, an alleged world price, or some other surrogate benchmark such as an "opportunity cost"). Yet as I've already explained, Pemex as ammonia producer pays for gas more than the price charged to other industrial users. In other words, the price Pemex pays exceeds the generally available price within Mexico. Consequently, natural gas is neither provided for ammonia production "at preferential rates," nor at a rate cheaper for a "specific . . . industry, or group of . . . industries." The allegedly "commercially unreasonable price" for gas also does not give rise to an export subsidy: it is not contingent upon export performance, and we have no reason to believe it operates to stimulate export over domestic sales.

Petitioner's major remaining allegation was that Mexico subsidizes ammonia by imposing a high export tax on natural gas, but no export tax on ammonia (although the Government imposes a lesser gross revenue tax on ammonia, but not gas). In theory, the high tax on gas exports discourages such exports and encourages the domestic sale and use of natural gas, which could in turn stimulate production of goods derived from gas, including ammonia. In practice, actual prices would depend on a complicated interaction of domestic and international supply and demand elasticities and substitution effects. (We have no evidence that the Mexican government performed such a complicated analysis.) In any event, increased production would not necessarily stimulate export sales for ammonia over domestic sales. In addition, the exemption from an export tax for ammonia is not in any way contingent upon export performance by Mexican ammonia producers. The export tax scheme therefore does not confer an export subsidy. Nor does it confer a domestic subsidy, since the standard industrial price for natural gas within Mexico is not provided only to a "specific * * * industry, or group of * * * industries." It is instead generally available to industries within Mexico, and used by a wide spectrum of industries.

For all these reasons, the Department concluded that Mexico has not provided countervailable benefits through a selectively available upstream subsidy to its ammonia industry through natural gas pricing and tax policies.

III. SOFTWOOD LUMBER PRODUCTS FROM CANADA

Let me turn now to our CVD investigations of softwood lumber products from Canada. On May 24, the Department issued final determinations that such products receive only de minimis subsidies (less than .5 percent ad valorem), so the cases were terminated.

The main allegation—accounting for over 95 percent of all subsidies alleged—was that the Canadian federal and provincial governments give the Canadian "forest products industry" a domestic subsidy through their stumpage programs. Stumpage programs are the systems by which individuals and companies acquire rights to cut and remove standing timber from government forest lands. We decided that stumpage programs do not confer a countervailable domestic subsidy for the following reasons.

A. Stumpage programs are not provided to a "specific group of industries"

First, stumpage programs are not provided only to a "specific * * * industry, or group of * * * industries." Rather, they are available within Canada on similar terms regardless of the industry or enterprise of the recipient. The only limitations as to the types of industries that use stumpage reflect the inherent characteristics of this natural resource and the current level of technology. As technological advances have increased the potential users of standing timber, stumpage has been made available to the new users. Any current limitations on use are not due to activities of the Canadian federal or provincial governments.

Nominal general availability of a program does not necessarily suffice to avoid its being considered a possible domestic subsidy. The Department further determined that stumpage is used within Canada by several groups of industries. In this regard, we noted that under the classification systems of both Canada and the United

States, the lumber and wood products industries, the pulp and paper industries, and the furniture manufacturing industries constitute at least three groups of industries.

In view of its general availability without governmental limitation and its use by wide-ranging and diverse industries, we determined that stumpage on Canadian government lands is not provided to a "specific group of * * * industries." Therefore, even if Canadian stumpage programs had conferred a domestic subsidy, they would not have been countervailable since they are not provided for "a specific group of * * * industries."

B. Stumpage programs do not confer a domestic subsidy

The Department further decided that stumpage programs do not confer a domestic subsidy. Subsections 771(5)(b)(i)-(iv) are mutually exclusive. Where a particular subsection clearly covers a given program, the determination whether that program is a subsidy must be based upon the standard provided in the relevant subsection. Stumpage programs clearly involve the provision of a good (raw timber), and thus clearly fall within subsection (ii).

The standard contained in subsection (ii) is "preferentially." Thus, the issue is whether the good is provided on terms more favorable to some within the relevant jurisdiction than to others within that jurisdiction. In this context, it does not mean "inconsistent with commercial considerations." a distinct term used in subsection 771(5)(b)(i) (which applies only to the provision of capital, loans, or loan guarantees). We found that stumpage programs do not provide raw timber at preferential rates.

As I have already indicated, we felt that only subsection (ii) applied to stumpage programs. Yet even if subsection (iv) also applied, we determined that Canadian stumpage programs do not "assume" a cost of production. The term "assumption" can only refer to government activity which relieves an enterprise or industry of a pre-existing statutory or contractual obligation. If interpreted more broadly, subsection (iv) would embrace all the activities described in preceding subsections (i)-(iii), because the activities described in those subsections could all be regarded as activities which reduce or absorb—and thereby arguably "assume"—costs of production. Such a broad construction of the term "assumption" would make subsection (iv) largely redundant of subsections (i)-(iii), and would therefore be unreasonable.

Under our interpretation of the term "assumption," stumpage programs do not assume a cost of production, because the Canadian governments do not relieve producers of any pre-existing statutory or contractural obligations. To the contrary, the governments impose a cost for the stumpage, which they have owned themselves for well over a century. These imposed costs include not only cash payments for stumpage, but also one or more other costs, such as ground rents, forest management plans, silviculture and road building.

Even if "assumption" were construed more broadly, we determined, based upon the record of these investigations, that Canadian stumpage programs have not effectively "assumed" a cost of production. Petitioner claimed that we should compare prices for Canadian and U.S. stumpage, and conclude that lower Canadian prices result from governmental assumption of production costs. We disagreed. First, we do not believe that cross-border comparisons should be used to establish commercial benchmarks, for reasons I will subsequently describe.

Second, there is not a unified North American market or price for stumpage, because each individual stand of timber is unique due to a variety of factors, such as species combination, density, quality, size, age, accessibility, terrain and climate. Stumpage prices vary substantially both regionally and locally within Canada and the United States, even within a given mill's timber supply area. Comparing Canadian and U.S. stumpage prices would be arbitrary and capricious in view of: (1) the wide differences between species composition; size, quality, and density of timber; terrain and accessibility of the standing timber throughout the United States and Canada; (2) the additional payments which are required in many provinces in Canada, but not generally in the United States; (3) the fact that in recent years, prices in national forests in the United States have been bid anywhere between two to five years in advance of cut; and (4) the fact that in recent years the U.S. Forest Service has restricted the supply of timber in certain national forests due to budgetary and environmental constraints.

Even if we had compared U.S. and Canadian stumpage prices, we noted in our decisions that the record of those investigations included studies showing that once appropriate adjustments are made to take into account the differences in quality, accessibility, as well as additional cash payments and in-kind services, Canadian prices for standing timber do not vary significantly from U.S. prices. Indeed, in some cases the Canadian price may be higher. Therefore, even if one were to use U.S. prices as a benchmark, there was evidence in the record establishing that the Canadian governments do not assume costs of production through their stumpage programs.

In the absence of a market price for stumpage with which the Canadian stumpage prices may reasonably be compared, we could have alternatively determined whether Canadian stumpage prices reflect "true market value," as petitioner suggested. The value of stumpage derives from a number of factors, including the price of the end products made from it, and not from any intrinsic value of the standing timber. One method of establishing stumpage prices, which is used in British Columbia (BC) and some parts of the United States, is to calculate its residual value based upon the end-product price. Under the residual value approach, the seller makes allowances for normal profit and risk factors and deducts manufacturing costs from the end-product price to determine the minimum price for stumpage below which it will not sell.

Residual valuation constitutes a reasonable method for establishing stumpage prices. Therefore, it cannot be said that prices charged in BC for stumpage do not reflect "true market value," as alleged by petitioner. Accordingly, we could not find that stumpage programs in BC "assume" a cost of production, even if that term were interpreted broadly.

For all the above reasons, we determined that Canadian stumpage programs do not "assume" a cost of producing the products under investigation.

In summary, we found that there were no countervailable benefits on many grounds: no benefits to a "specific group of * * * industries;" and no domestic subsidy, since no provision of a good at preferential rates and no assumption of a cost of production.

IV. PROPOSED AMENDMENT TO CURRENT LAW

We believe the Department of Commerce properly decided the Canadian softwood and Mexican ammonia cases under current law. More importantly for purposes of this hearing, we believe that the results reached are appropriate and should not be reversed by the types of amendments proposed, for the following reasons.

First, as reviewed earlier, domestic subsidies are potentially countervailable only if provided to a "specific enterprise or industry, or group of enterprises or industries." Generally available domestic subsidies do not distort the allocations of resources within an economy. Absent any distortion in resource allocation, domestic subsidies merely assist the economy as a whole and not particular industries or sectors.

Second, we must remember that any precedent we set will likely be emulated by our trading partners. Since U.S. natural gas prices are still regulated, U.S. products—such as textiles and petrochemicals—made using natural gas and exported would be targets for retaliation and CVD proceedings abroad. And it is by no means guaranteed that our trading partners would be as careful in their drafting as the subcommittee is attempting to be.

Third, eliminating or qualifying the requirement that a domestic subsidy be provided to a "specific group of * * * industries" would mean that in most cases we would brand as "unfair" foreign government practices which do not distort resource allocations either within its own economy or vis-a-vis other economies. We would be asked to sit in judgment on the fairness of our trading partners' practices; the "unfairness" label would itself be perceived by our trading partners as an unfair intrusion into their sovereign and internal policies and practices.

Fourth, we do not think it is fair to preclude other countries with an abundance of natural resources from capitalizing on the comparative advantages of such resources for their economic development. The proposal before the Subcommittee would force such natural resources to be sold at prices established by less competitive producers.

Fifth, the proposed amendments would depart significantly from the international consensus on what constitutes a subsidy. It is inconsistent with U.S. obligations under the General Agreements on Tariffs and Trade. The United States is already the most aggressive enforcer and interpreter of the Subsidies Code and of domestic CVD laws. We believe that further distancing the U.S. ahead of its trading partners in this regard is not in our overall best interest in seeking greater discipline on the use of subsidies.

Mr. Chairman, while we have concerns with respect to the amendments which have been suggested, we look forward to continuing to work closely with you in addressing this issue.

28-466 O—83——3

I would be happy to respond to any questions.

Chairman GIBBONS. We certainly respect your views, but I just want to remind the executive branch that all of the powers that they have, that they use in international trade, are not inherent powers. They are powers delegated by the Congress under the Constitution to the executive branch. I realize we can't change the law without the President signing it unless we have two-thirds vote, but that is a constitutional restriction.

Let me say I am not going to quarrel with you about the Canadian stumpage case. I know it is somewhat analogous here. I am not prepared to talk about that one.

Where does this test—and I assume this was the controlling and overriding test—what is the genesis of this test?

Mr. HOLMER. Mr. Chairman——

Chairman GIBBONS. A domestic subsidy to be objectionable must be provided to a specific enterprise or industry or group thereof, rather than generally available throughout the domestic economy.

Where did that language come from? What is it based on?

Mr. HOLMER. Well, it is based really on two things. One, it is based on the attitude that I expressed in my testimony that a countervailable domestic subsidy should be one which really attempts to give a special benefit to a specific industry or to a group of industries within the same economy and thereby distorts the allocation of resources within that economy. That is No. 1.

Number two, my understanding is that this is a principle that evolved through the course of the Treasury Department's interpretation and administration of the countervailing duty law.

Chairman GIBBONS. That is the reason why we took it out of the Treasury Department.

You know, we didn't expect you to copy all their bad habits.

Mr. HOLMER. We believe in this area——

Chairman GIBBONS. I guess we should have told you that a little more clearly than we did in the statute. But as I have said earlier, for years they didn't do anything.

Mr. HOLMER. Well——

Chairman GIBBONS. They never decided anything, never did anything; they just rocked along over there and finally right here in this room we told them, "You are out of the picture. We are going to move it over to Commerce where we hope we can get some better results."

Now, is this a practice? Is it a law? Is it based in GATT? Where does it come from?

Mr. HOLMER. Well, for better or for worse, it was the practice. And at roughly the same time when the responsibility was transferred from Treasury to the Department of Commerce, the Congress in the Trade Agreements Act of 1979 ratified the existing Treasury Department practice and stated with great specificity in the statute the standard we should use in cases such as this.

The statutory language is extremely specific in stating that you have countervailable domestic subsidies when they are provided to a specific enterprise or industry or groups of enterprises or industries. Based on the specificity of that statute, we felt that the Congress provided no flexibility with respect to how the statute could be administered.

Chairman GIBBONS. If we repeal that language specifically and substitute for it some other language, language we think more appropriate, you will follow the new language, I assume?

Mr. HOLMER. As administrator of the antidumping and countervailing duty laws, I will do everything I possibly can to follow the statutory direction given to the Department of Commerce by the Congress, yes, sir.

Chairman GIBBONS. Is there anything that we would do to change the language from what it is there to an export price; or where there is no export price available, then the fair market value? Is that in violation of the General Agreement on Tariff and Trade, or is it in violation of the Subsidies Agreement we have entered into?

Mr. HOLMER. Mr. Gingrich would like to address that issue.

Mr. GINGRICH. In response to that question, Mr. Chairman, I think we have to look at what a subsidy is. A subsidy is a decision on distribution of national wealth by a government or administrative authorities.

Chairman GIBBONS. I know what a subsidy is. Just answer the question. I know what a subsidy is. I know that.

Mr. GINGRICH. We have agreed with our trading partners that certain things will be countervailable, and we have defined those to the extent we can. We never were able to reach agreement beyond the language which is now implemented in domestic law with respect to specific subsidies.

I guess what I am saying is that if we redefine our subsidy law to go beyond where we are now, we will not have coverage in the GATT or in the Subsidies Code. We would be subject to challenge. And while we would obviously defend the actions of the U.S. Government to the best of our abilities, we couldn't predict the outcome.

Chairman GIBBONS. Let me repeat my question.

The language I have outlined here, the export price, or where there is no export price available then the fair market value, is that a violation of the General Agreement on Tariffs and Trade?

Mr. GINGRICH. It is not in conformity with our Subsidies Code obligation as the Subsidies Code interprets the GATT.

Chairman GIBBONS. Go over that again.

Mr. GINGRICH. It is not in conformity with our Subsidies Code obligations.

Chairman GIBBONS. I missed the second word.

Mr. GINGRICH. It is not in conformity with our Subsidies Code obligations.

Chairman GIBBONS. That isn't the question I asked. I asked you: Was it a violation of the code, yes or no?

Mr. GINGRICH. The code doesn't deal with it. Specifically, no. It is not a violation; it is just——

Chairman GIBBONS. That is what I wanted to hear. I got it. It is clear now.

Now, was your statement covering both the code and GATT, or what?

Mr. GINGRICH. The code interprets the GATT provisions.

Chairman GIBBONS. So it is not a violation of either the GATT or the code, the Subsidies Code?

Mr. GINGRICH. The code does not contemplate that we can——

Chairman GIBBONS. I know that. You told me that. I am asking you whether it is a violation of it?

Mr. GINGRICH. Mr. Chairman, no, not in that it does not deal with indirect subsidies. But we would be in violation of our code obligations if we imposed countervailing duties under the formula that you are talking about.

Chairman GIBBONS. What kind of code obligations do you have that I don't know about?

Mr. GINGRICH. The code says you cannot impose a countervailing duty except as agreed to in provisions of the code. This is outside the provisions of the code. We adhered to that code and implemented it in domestic law.

Chairman GIBBONS. Mr. Hance.

Mr. HANCE. Thank you, Mr. Chairman.

In looking at your testimony over on page 11, you say, "* * * we believe that the results reached are appropriate and should not be reversed by the types of amendments proposed * * *"

You know, I think this makes it abundantly clear to me that we need to write a statute that you can't misinterpret. We just have to make it so plain that the L'il Abner people could follow it; that even he would interpret it clearly.

I think we need to look at your past action, like on the oil country tubular goods. The United States signed a 3-year agreement with the European countries and they violated it in 6 months. You all will still—thank goodness—be visiting with me about it. But it seems like we are always visiting. I have always been one for free trade, but I will tell you what is happening with the American public.

It is kind of like at the State Department. They have an Asian desk and a European desk and an African desk. In the Commerce Department you have the same thing. The public is going to wonder if we can get an American desk over there.

I will tell you, the attitude that comes down from the Department really concerns me—I just think it reconfirms my thoughts and my beliefs that if we write something, we have to write it very tight.

You talk about retaliation. We understand retaliation. What do you do when there is a subsidy going into an industry, like cement or like carbon black, and our people cannot compete, and other countries continue to subsidize? What do you do? Should we tell our people, "Tough luck; you should be in some area where there is not a subsidy"?

What would you say to that? What would you say to the man that is laid off in the cement industry?

Mr. HOLMER. If I could, I would like to respond to a couple of items you made as you walked your way through.

First, with respect to the oil company tubular goods, I look forward to meeting with you, and we are doing more than visiting with the European folks on that. We have had strong words with them on that subject, and we are awaiting——

Mr. HANCE. I would like copies of that.

Mr. HOLMER. We have correspondence.

We went to Brussels to express our strong concern with respect to the present situation. But we can pursue that more later.

Mr. HANCE. That may help a little if somebody on the trade staff were invited along, maybe. It would give us a little confidence you were fighting for us every once in a while.

Go ahead.

Mr. HOLMER. It would be useful for us to have a chance to pursue that issue at the session being set up with your staff for next week, along with other issues.

With respect to having a statute that is so clear it can't be misinterpreted and a statute that is very, very tight, we believe you have that presently with respect to the statute enacted in 1979. It is very clear from our perspective that it is very tight, and we believe we have accurately and fairly interpreted it.

Certainly it is within the power of this subcommittee to propose changes with respect to that statute that would change it and would make it even more tight and would direct Commerce on a different course. We believe that doing that, at least based on the present proposals we have seen, would be ill-advised for the reasons I have outlined in my testimony.

We do not sit here and have a lack of sympathy for the concern that you have and the concerns that your constituents have. The present situation does present a very hard case. For better or for worse, I think this is a classic case of the principle that hard cases can often make bad law.

We are concerned that once you get on the slippery slope of departing from the principle of general availability, there is no telling where it will lead—not necessarily within this country but with respect to our trading partners. That is one of the principal bases for our concern with respect to the proposals you are considering.

Mr. HANCE. That is well and good, but I am afraid that the attitude is that someone may get offended, so we better do nothing. That is what you are saying.

My last question was, What do you tell the cement worker that was laid off?

Mr. HOLMER. I believe you tell the cement worker that what is at issue is not a subsidy under the present law or with respect to the international consensus as to what is a subsidy. What is the problem is a market access problem—the lack of access of U.S. ammonia producers or carbon black producers or others to raw materials in other countries. That is an issue, it seems to me, that can be addressed through a statute other than the countervailing duty law without getting into the problems we envisage if you attempt to change the countervailing law to address this problem.

Mr. HANCE. If we don't change the countervailing duty law, then how do we address the problem where foreign producers are getting their energy cheaper than we get our energy.

Mr. HOLMER. One of the ways to do it in terms of a problem of access is look at it through section 301. Mr. Gingrich would like to discuss that.

Mr. GINGRICH. Congressman Hance, the 1974 version of 301 contained market access, the notion of market access. That language was eliminated from the 1979 version but the committee reports both clearly state that everything covered by the 1974 act is covered by the 1979 act.

So access to raw materials is covered. You get into the very interesting question of how far the U.S. Government is willing to go in saying that a sovereign decision to restrict the distribution of its natural resources is unfair.

We have an Alaskan oil embargo. We have very tough questions there. Mr. Holmer is right, it is addressed under 301, or, you can go under 201.

Mr. HANCE. Have you all done so? Have you addressed it under either of those?

Mr. GINGRICH. No, it has not. It has not been brought to us by petition under either statute.

Chairman GIBBONS. There is nothing to stop you from doing it under your own motion.

Mr. GINGRICH. We would be perfectly willing to look at it.

Mr. HANCE. Why don't you do it today?

Chairman GIBBONS. Why didn't you do it a year-and-a-half ago?

Mr. HANCE. One of the problems is that you need to show some leadership in this area. You should try to solve some of these problem instead of waiting until they shape up into a crisis situation.

Thank you, Mr. Chairman.

Chairman GIBBONS. Mr. Frenzel.

Mr. FRENZEL. Mr. Chairman, I apologize for being in and out of here. I have another markup, we are waiting for the Democrats to caucus and it is a pleasure to know there is another group as loused up as much as the Republicans.

Chairman GIBBONS. At least.

Mr. FRENZEL. I want to apologize to the witnesses for not being here. I understand you were asked, Claud, whether this language would be in conformance with our GATT obligations and your clearcut response was maybe.

Chairman GIBBONS. No, no, he said yes.

Mr. FRENZEL. Do you want to say it for me?

Mr. GINGRICH. Yes, Congressman.

Article 1 of the Subsidies Code says that signatories shall take all necessary steps to insure that imposition of a countervailing duty is in conformity with provisions of article VI of the General Agreement and the terms of this agreement; that is the Subsidies Code.

What I was saying was that to countervail against what would be an indirect subsidy would be outside that which has been generally deemed by the contracting parties and by the signatories to the Subsidies Code as being a countervailable indirect subsidy.

Mr. FRENZEL. And in the past there have been items which you and I thought were in conformance with the GATT and when the complaint was taken to a panel we have lost, is that true or not?

Mr. GINGRICH. I am absolutely certain that that is the case.

Mr. FRENZEL. So the fact is that we probably don't know until we have a case?

Mr. GINGRICH. We certainly would not know for sure whether or not we would be in conformity until a case was brought and decided.

Mr. FRENZEL. As the chairman knows I am nervous about our writing law around the worst cast at the moment that is bothering us. Is it not possible for Mr. Hance's distressed cement interests to take a 201 case based on a search?

Mr. GINGRICH. It certainly is. There are regional industry provisions that are covered.

Mr. FRENZEL. Have they done that?

Mr. GINGRICH. No, they have not.

Mr. FRENZEL. Instead they want the law to be changed to fit the current situation, that is the distressed situation?

Mr. GINGRICH. I am told that the people Mr. Hance refers to support the language before the committee.

Mr. FRENZEL. It is an understandable reaction on their part I am sure, but I am really very nervous about writing something into the law that has future implications which we don't understand. We are exporting some raw materials. We would like to export a lot more coal, for instance. We think we are the world's Saudi Arabia for coal.

What happens with mirror legislation to federally financed port and waterways improvements under the export of coal? It would be countervailable under this law, would it not?

Mr. GINGRICH. It certainly could be under the broad language being discussed.

Mr. FRENZEL. How about the black lung benefits paid by the Federal Government, that would be countervailable, I assume?

Mr. HOLMER. If this statute that is proposed were written by our trading partners precisely as it is presently being drafted by the subcommittee staff, there probably would not be a problem.

Chairman GIBBONS. That is right.

Mr. HOLMER. But we have no guarantee and little confidence that our trading partners would draft their statutes specifically to address our problem. They are going to draft statutes that are going to address their problems, and as they depart from the general availability standards, we have a fear they would get into the kinds of generally available programs you are discussing.

Mr. FRENZEL. I guess my problem is that I am not sure quite what the draft is we are talking about. We have a number of them before us as you know.

I don't know whether we are talking about the Moore draft or the committee staff draft or the staff draft as amended by the original Moore language. Which one are you saying we would be safe under?

Chairman GIBBONS. Before the witness answers that question, let me try to clarify the gentleman's legitimate question.

All of the alternatives that we have before us would require a finding, a finding by Commerce, that the controlled resource, or the artificially priced resource, constitutes a significant portion of the resulting products manufacturing cost.

It has got to be a significant portion. I don't imagine some harbor-deepening project would be a significant portion of a manufacturing cost of a product.

You know, I don't think any other things that the gentleman mentioned—and I know he mentioned them in good faith because he is concerned about this—but they have to be a significant portion of the manufacturing cost. They cannot be just an incidental thing. They also have to cause injury.

Mr. FRENZEL. Mr. Chairman, may I further inquire of the Commerce Department, didn't we go through this not on the countervailing but with an antidumping case on steel; and did we not include as part of the dumping housing subsidies granted to British steelworkers; and is that not a comparable sort of cost element?

Mr. HOLMER. Yes, in a countervailing duty case.

Mr. FRENZEL. Comparable to black lung.

Mr. HOLMER. I would have Ms. Bello respond to that.

Ms. BELLO. Mr. Frenzel——

Chairman GIBBONS. We cannot hear you, could you pull that mike real close.

Ms. BELLO. The only allegations I recall in the 1982 carbon steel cases about subsidized housing were in Italy rather than the United Kingdom; and they were made in the context of the subsidy cases, not the dumping cases.

Mr. FRENZEL. Would you take another look at the dumping case which was of course terminated.

Ms. BELLO. I would be happy to.

Mr. FRENZEL. And be prepared to advise by filling in the record for us.

Ms. BELLO. Yes.

Mr. FRENZEL. Thank you.

[The information follows:]

U.S. DEPARTMENT OF COMMERCE,
INTERNATIONAL TRADE ADMINISTRATION,
Washington, D.C., October 27, 1983.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, House of Representatives,
Washington, D.C.

DEAR CHAIRMAN GIBBONS: At the Trade Subcommittee's hearing on October 20, Mr. Frenzel asked how the Department of Commerce treated allegations of subsidized housing in our 1982 dumping investigations of certain carbon steel products from the U.K. I am writing to answer that question for the record, as requested by Mr. Frenzel.

In our Final Affirmative Countervailing Duty Determinations: Certain Steel Products from Italy (47 Fed. Reg. 39356), petitioners alleged that the Italian Steel industry benefits from housing allowances provided by the Italian government. We determined that such programs were not countervailable because Italian laws indicated that such allowances are generally available on equal terms to all firms in Italy, not just to firms in a particular industry, group of industries or region of the country.

In Appendix 3 to our Final Affirmative Countervailing Duty Determinations: Certain Steel Products from Belgium (47 Fed. Reg. 39304, 39324), we noted that the European Steel and Coal Community provides loans for residential housing for steel workers. These loans are for the construction or purchase of homes at highly concessionary one percent interest rates. Although they substantially benefit steel workers, we found no evidence that they indirectly benefited the employer steel companies as well by relieving them of certain labor wage costs. To the contrary, in many of the countries concerned we found high rates of unemployment reducing any upward pressure on wages. Moreover, we found no instance in which wage rates varied—depending upon the presence or absence of these loans to steel workers—either within a steel company or between steel companies. Therefore, we concluded that the hypothetical benefits conferred by the loans on employer steel company were too remote to be considered subsidies to those companies.

We applied these findings in, *e. g.*, our Final Affirmative Countervailing Duty Determinations: Certain Steel Products from Italy (47 Fed. Reg. 39356). One Italian steel company received ECSC housing loans for its workers at a particular facility. For the reasons described in Appendix 3, we did not countervail those loans. In our Final Countervailing Duty Determinations: Certain Steel Products from the United Kingdom (47 Fed. Reg. 39384), we found instead no evidence that such loans had been paid either to UK steel companies for disbursement to their workers or directly to United Kingdom steelworkers.

Our records in companion dumping investigations of certain steel products from various EC countries do not reveal any allegations that housing subsidies to steelworkers reduced steel producers' cost of production.

I hope this letter responds satisfactorily to Mr. Frenzel's question.

Sincerely,

ALAN F. HOLMER,
Deputy Assistant Secretary for Import Administration.

Mr. FRENZEL. I don't want to belabor this. You know, I am nervous about it.

Chairman GIBBONS. We are all nervous about it, Bill.

Mr. FRENZEL. This country has some iron, some minerals, some coal, and other products that get put into finished products and I don't want to expose us, that is all.

Chairman GIBBONS. I don't either, Bill.

Let me say, too, one, you must cause injury under this bill. I am just waiting for someone to say, oh, Mexico is not entitled to the injury test. Well, that is not my fault.

Two, it has got to be a significant portion of the manufacturing cost, the manufacturing cost now.

Then we try to figure out how you price this, how you put a price on the subsidy. We have heard from Mr. Gingrich, after I pulled on him real hard, that this is not a violation of the GATT or the Subsidies Code. As I say, and I repeat, and I will repeat ad nauseum, all I am trying to do is level the playing field.

Mr. FRENZEL. I am with you, Mr. Chairman, but I remember I said DISC wasn't in violation of the GATT either; a couple other people didn't agree with me, unfortunately.

Chairman GIBBONS. Well, I think——

Mr. FRENZEL. Mr. Chairman, I yield the rest of my time.

Chairman GIBBONS. Mr. Russo.

Mr. RUSSO. Thank you very much, Mr. Chairman.

I guess it is not a very easy task to come before the Congress on such an issue as this. But let me tell you I am a little buoyed by the chairman's reaction this morning. You are making Sam Gibbons more of a fair trader than free trader if I read him correctly. That is the problem you face with industries in this country and the problem you face with other Members of Congress.

You are adhering to the law so closely that you appear more concerned about what our trading partners' reaction is to what we do rather than worrying about what the reaction of the American people and industries and Members of Congress will be.

This is something you ought to be very sensitive to because I know you are trying to enforce the letter of the law but I think laws in this country are made so that they can be changed when we see a problem that needs to be addressed. Your only response is that if we do something our trading partners are not going to be able to pass a law as phrased as properly as we can.

My answer is who cares? I don't care. I am concerned about what we do as it relates to our own country. If other countries don't draft legislation properly aren't there certain actions we can take to let them know they are not drafting their measures properly? Why don't we react to what we do rather than anticipate what they might do and take care of the problems that require addressing in this country?

Do you have a comment on that?

Mr. HOLMER. I do.

Mr. RUSSO. I have a lot of other things to say so I will stop there.

Mr. HOLMER. I just wanted to be sure you were finished.

First, I do appreciate the comments that you have made. We have looked at this statute, and if you do look at the statute, it is one that is extremely detailed and extremely specific. I think in large part it is because the Congress wants to make sure that the law is accurately and fairly interpreted by the Commerce Department so we don't abuse discretion from Deputy Assistant Secretary to Deputy Assistant Secretary or from administration to administration.

Because of the specificity with respect to that statute, we feel that in the *Carbon Black* case and other cases, there was no choice but to reach the conclusions that we did.

I think that you will be hearing later on in the course of this hearing from other U.S. domestic industries that have very great concerns with respect to what the effect of this change will be with respect to their businesses.

We think that that is a very important consideration that this subcommittee needs to keep in mind.

Mr. RUSSO. I agree. I am not taking sides on this issue. But the thing that irritates me is we always seem to be worrying about what our trading partners will do, how they will react to something we need to do here, whether it is steel, ammonia, or whatever product we discuss.

One of the things that frustrates the American people, thinking back to my district, is that they don't think the Commerce Department is created to protect American commerce; they think it is there to protect foreign countries, because it takes so long for the Commerce Department to do anything so that by the time you act the industry that needs help is gone.

So their industry comes to the Congress and says I will not file that 201 suit because by the time I file it and Commerce goes through all their channels I will be out of business. My only recourse is go to Congress and get an amendment passed to open Commerce's eyes.

I have people in my district telling me that what we need to do is replace people in Commerce with steelworkers, cement workers, and automobile workers and get the academics out of Commerce and put in the people who suffer under these laws, where they can make the changes.

I am not trying to be critical; you have a tough job; the line you have to walk is not easy. You have to understand that out in the districts there are a lot of things happening. Kent Hance made it clear, a lot of people want to know where the American desk is in Commerce. It is a legitimate problem we face.

I saw the chairman work very hard to try to get a response to his question. And if the chairman of the Subcommittee on Trade has a tough time getting responses from you, just imagine someone else who doesn't have the clout if he has to deal with you, how they must feel when they leave your office? They come to us and say you don't care about us.

The example we are witnessing this morning is a good reason why all these trade remedy laws are coming up; we will make it easy for you to act; we won't give you very much discretion. That may not sit well with Mr. Frenzel or with other Members but we may not be able to control the Members of Congress from saying, give the Commerce Department very little discretion.

When we give you flexibility, you do what you want to do; you don't respond to the needs that must be addressed by the Members. I think we may eliminate any role for the Commerce Department in international economic affairs. We will just do it here because we cannot rely on you anymore.

I think that may happen.

Mr. HOLMER. I appreciate your comments. The only response I would make is that one of the reasons why we have been eager to participate with the chairman and other members of the subcommittee with respect to trade law reform efforts is because we are eager to undertake an effort to rewrite the law to make it less expensive for those who are seeking relief under it, to make the relief more certain, make the process more efficient, and generally make it more effective.

I hope that that can be the result of this effort.

Mr. RUSSO. I certainly hope so because we need to do something. I know the chairman and Mr. Frenzel are working hard at it, and they make a lot of good arguments but sometimes you have Members out there saying, look, I listened to that argument and things are just not happening. Look what happened to Lone Star Steel, among others. I can point out examples in my own district.

Some of the arguments that Dave Roderick uses involving United States Steel, why they went to make the steel with the Europeans, because we can't win on our trade remedy laws. It is terrible to hear that, isn't it?

I don't have any other questions, Mr. Chairman.

Chairman GIBBONS. Thank you, sir.

Thank you, gentlemen.

Mr. HOLMER. Thank you, Mr. Chairman.

Mr. GINGRICH. Thank you.

Chairman GIBBONS. We have a panel of the Ad Hoc Committee of Domestic Nitrogen Producers, Mr. Jaquier, executive vice president of W. R. Grace & Co.; Mr. Gerstell, president and chief operating officer for California Portland Cement Co.; Mr. Bronson, president of Moore-McCormick Cement Co., Inc.; Mr. McCoy, owner of the Valley Builders Supply; Mr. Sam Coco, Jr., senior vice president of Cabot Corp.; and Mr. Newhouse, counsel for Hammond Lead Products Co.

First, we will have Mr. Jaquier.

STATEMENT OF L. L. JAQUIER, EXECUTIVE VICE PRESIDENT, W. R. GRACE & CO., ON BEHALF OF THE AD HOC COMMITTEE OF DOMESTIC NITROGEN PRODUCERS, ACCOMPANIED BY DONALD V. BORST, SENIOR VICE PRESIDENT, CF INDUSTRIES, INC., AND D. W. CALVERT, CHAIRMAN, PRESIDENT, AND CHIEF EXECUTIVE OFFICER OF AGRICO CHEMICAL CO.

Mr. JAQUIER. Mr. Chairman, I am L. L. Jaquier, executive vice president of W. R. Grace & Co., and its agricultural chemicals group executive. On my right is Don V. Borst, senior vice president of CF Industries, Inc., a company owned by the major agricultural cooperatives in the United States structured to provide fertilizer to farmer patrons. On my left is D. W. Calvert, chief executive officer of Agrico Chemical Co.

Mr. Borst and Mr. Calvert and I appear on behalf of the Ad Hoc Committee of Domestic Nitrogen Producers, a coalition of 12 nitrogen producers in the United States. Mr. Nolan Hancock of the Oil Chemical and Atomic Workers International Union is also with us and I would like to point out that the Labor Industry Coalition on International Trade is a supporter of the position of the ad hoc committee.

Mr. Richard R. Rivers, our trade counsel, is also with us and will be pleased to answer any GATT-related questions.

The ad hoc committee represents fertilizer plants employing the latest technology. These plants are efficiently operated and well located with respect to natural gas supplies and with respect to the U.S. market. We represent a strategic free enterprise petrochemical industry whose life is threatened by state-owned monopolies subsidized by artificially low energy feedstocks and other product input prices which are well below fair market values.

These state-owned enterprises have built large capacities for producing ammonia, specifically for export, and are penetrating world markets and the U.S. market by setting prices at or below market producers' production costs. This tactic has driven U.S. companies out of the market and if continued will result in additional destruction to the U.S. industry.

Two-tier pricing of fungible commodities like natural gas and oil is definitely a subsidy. Two-tier pricing problems arise primarily from nonmarket economies and from nonmarket monopoly sectors of mixed economies where conscious Government action is taken to force prices below free market levels in order to penetrate world markets.

Such pricing tactics are clearly a subsidy and are indistinguishable from a direct cash payment to foreign producers by their governments. The amount of the subsidy is the difference between the free market energy price and the price at which the government supplies its own state-owned monopolies.

If Congress acts against two-tier practices free market forces will dictate the future of nitrogen fertilizer production in the United States. If Congress does not act, political decisions outside the United States will control the vital supply of nitrogenous fertilizer to the American farmer.

Under current practices, the U.S. nitrogen industry will be unable to supply U.S. nitrogen requirements long-term. The industry has no basis for future capital investment or future commitments to purchase gas. The committee should also recognize that our experience will not be unique but will spread throughout the entire petrochemical industry and other energy-intensive industries such as cement and carbon black which are also testifying here today.

The committee has requested recommendations on how to measure the level of subsidy in two-tier pricing. The best standard is one that utilizes actual prices negotiated in the free market between a willing buyer and willing seller.

For example, today there is a market clearing price for natural gas in the United States, the level of which even Commerce could determine easily. This market clearing price establishes a price level at which Mexican natural gas could be sold in a free market. The difference between this price netted back to the wellhead, that is the selling price less transportation cost, would establish the actual value at the wellhead of Mexican gas.

The difference between this established value and the subsidized price at which the Mexican Government is supplying its state-owned monopoly industries, also netted back to the wellhead, would be the level of subsidy per thousand cubic feet of gas. In the case of ammonia this difference times 37.5, it takes 37,500 cubic feet of gas to produce 1 ton of ammonia, would fairly measure the level of subsidy per ton of anhydrous ammonia.

I would like to read to the committee an English translation of the official Mexican industrial development plan. The Mexican industrial development plan states the intent of two-tier pricing most clearly:

> This plan is complemented by an explicit policy of maintaining internal prices of energy sources for industrial use below that of the international market. This allows for the strengthening of industry by giving it a substantial margin of protection via inputs. In contrast to other forms of protection which tend to make such costs more expensive and access to external markets more difficult, this mechanism constitutes a direct incentive to exports.

Chairman GIBBONS. What is the source of that?

Mr. JAQUIER. The source of that is the published Mexican industrial development plan which is an official Mexican Government policy, perhaps even law.

I think that clearly explains the problem which we as free enterprise producers face, Mr. Chairman.

I thank the committee for this opportunity to testify. We have submitted written testimony which expands on the contents of this summary. We will be pleased to answer any questions you may have.

[The prepared statement follows:]

STATEMENT OF L. L. JAQUIER, EXECUTIVE VICE PRESIDENT, W. R. GRACE & CO., DONALD V. BORST, SENIOR VICE PRESIDENT, CF INDUSTRIES, INC., D. W. CALVERT, CHAIRMAN, PRESIDENT, CEO, AGRICO CHEMICAL CO., ON BEHALF OF DOMESTIC NITROGEN PRODUCERS' AD HOC COMMITTEE

Mr. Chairman and members of the committee, I am L. L. Jaquier, Executive Vice President of W. R. Grace & Co. and Agricultural Chemicals Group Executive. With me today are Donald V. Borst, Senior Vice President of CF Industries, Inc., which is a company organized by agricultural cooperatives to provide fertilizer to their farmer patrons; and D. W. Calvert, Chairman and Chief Executive Officer of Agrico Chemical Company. We are representing the Ad Hoc Committee of Domestic Nitrogen Producers, which is a coalition of twelve producers of ammonia and nitrogen fertilizers organized to address the increasing inability of U.S. fertilizer producers to compete with subsidized ammonia and urea imports from State-owned producers in certain countries.[1]

CF Industries, Inc. and the Ad Hoc Committee have previously presented testimony to this Subcommittee on March 17 and May 4, 1983, respectively on this problem and will not repeat that here today. Today, we will concentrate on the two key

---

[1] The members of the Ad Hoc Committee are Agrico Chemical Co., American Cyanamid Co., Center Plains Industries, CF Industries, Inc., First Mississippi Corp., W. R. Grace & Co., International Minerals & Chemicals Co., Mississippi Chemical Corp., Olin Corporation, Sohio Chemical Company, Terra Chemicals International, and Wycon Chemical Company.

issues presented by the Subcommittee for this hearing: That government two-tier pricing of natural resources constitutes a government bounty or grant—a subsidy—which should be countervailable under U.S. trade law; and, how it should be measured. We will concentrate our testimony on the example of how-tier pricing of natural gas provides an upstream subsidy for the production of petrochemicals like ammonia.

The essential facts are relatively simple. Since 1973, the governments of hydrocarbon rich countries have gotten directly, or indirectly through government owned or controlled enterprises, into the business of producing oil and natural gas, and various primary and secondary derivatives, including refined petroleum products, nitrogen fertilizers and other petrochemical products. Many of these countries export oil and some derivative products to world markets. Some are able to export gas by pipeline to major contiguous markets, for example, like the Soviet Union to Western Europe and Mexico and Canada to the United States. Some gas-rich countries are not able to export gas due to geographic location. The proposed amendment is not applicable to this latter group. that is an important distinction.

Free enterprise petrochemical producers are under attack by government owned, operated and subsidized producers—both oil and gas producers and petrochemical producers. Nonmarket economies and nonmarket segments of mixed economies are distorting world export markets and, more importantly, U.S. domestic markets. Our production costs are set by markets. Their production costs are set by the government themselves. We have to recover all our costs to stay in business. They do not. We have to make a profit—a return on our investment. They do not. We cannot compete with those governments.

Perhaps nothing can be done about state trading practices in world markets. But the Congress can and must do something about unfair state trading practices in our markets.

WHY TWO-TIER PRICING OF NATURAL RESOURCES IS A SUBSIDY

Now, why is two-tier government pricing of natural resources, like oil and gas, a subsidy? Under a two-tier pricing scheme, the foreign government sets one artificially low price for its industrial users of gas and a much higher export price for everyone else.

Basicially, subsidy is an advantage conferred by a government—not the marketplace—on its producers, which enables them to sell their products on a more favorable basis than competing producers in the same market. It is something a government does to give its producers more favorable terms than those which would be commercially available to those same producers on world markets.

The Soviet Union is also a principal user of the two-tier pricing scheme today through its high gas export price to Western Europe and a low price to its own petrochemical plant. The debate on this amendment has focused on Mexico because of its geographical location and its gas exports directly to the United States. This testimony thus focuses primarily on the Mexican situation.

PEMEX, the Mexican Government oil, gas and petrochemical producer, clearly gets its gas to make and export ammonia on much more favorable terms than would be commercially available to PEMEX if it were selling all of its gas freely in the market—domestic or export—and then using it for ammonia at the resulting market price.

If PEMEX sold all of its gas at its export price and the Mexican Treasury then wrote checks to Mexican industrial users to reduce their cost to $1.00 per thousand cubic feet, would that be any more or less a subsidy than charging a lower price to those producers in the first instance? Of course not, but that is the current result under our countervailing duty laws.

Two-tier pricing is a subsidy because it specificially and artifically lowers the production costs for energy intensive industries by direct government action. It gives them such an advantage that few U.S. producers can compete with them in the U.S. market. Competing producers cannot buy Mexican gas at the same low price. We are required to pay three to ten times more. We want to emphasize again. It is the government setting the price differential directly—not the marketplace. Gas at the lower tier price is cheap because the government says so, not the market.

Two-tier pricing of gas confers no significant export advantage on producers that use very little gas for energy. It confers an enormous advantage on energy intensive industries like petrochemicals. The Mexican Industrial Development plan states the intent of this policy most clearly.

"This plan [the IDP] is complemented by an explicit policy of maintaining internal prices of energy sources for industrial use below that of the international market. This allows for the stengthening of industry by giving it a substantial margin of protection via inputs. In contrast to other forms of protection which tend to make such costs more expensive and access to external markets more difficult, this mechanism constitutes a direct incentive to exports."

The Commerce Department says this is a domestic subsidy, and so long as the foreign government makes that subsidy generally available to all industrial users—and not to just a few—it is not countervailable. The argument is that the law must draw a line between traditional government services, policies and actions that benefit the economy as a whole and those that benefit specific groups of industries and distort trade.

The problem with such general principles is always one of degree. A direct cash grant to a specific company to export its product is clearly a trade distorting subsidy. Government support of public education clearly is not. The extreme cases are always easily identified. The problems arise from cases falling in between. There is no precise formula—such as specific industry subsidies or generally available subsidies—that will allow the Commerce Department to always draw a clear line. If a government wants to confer an advantage on exports of energy intensive industries—because it has alot of oil and gas—it can clearly do so without giving a specific export grant to a particular company or group of companies.

Some reasonable exercise of judgment has to be applied. It is like the famous comment of a Supreme Court Justice on pornography—you know it when you see it.

A review of exactly how the process works is the easiest way to see the subsidy. The governments of certain gas exporting countries have set two different prices for gas. They export gas at prices slightly below the BTU value of OPEC crude oil prices—$4.40 per thousand cubic feet (mcf.) currently in the case of Mexico. They sell gas to their domestic industrial users at much lower prices. In the last year, the Government of Mexico has set the industrial use price in Mexico at the dollar equivalent of 46¢ to $1.02 per mcf.

The gas price advantage of PEMEX—which is the single, government monopoly producer of both the gas and basic petrochemicals in Mexico—has been as much as $3.00 to $4.00 per mcf. in round numbers. It takes approximately 37,500 cubic feet of gas to make each ton of ammonia. This gives PEMEX a production cost advantage of $113 to $150 per short ton compared to their export gas price. Over the last year (October 1982—September 1983), PEMEX has sold ammonia delivered C&F to Tampa on the U.S. Gulf Coast at $120 per short ton.

The weighted average cost for all U.S. producers, including those with old low cost gas contracts, would be approximately $3.00. The weighted average price for current gas contracts, dropping out the low cost gas contracts made in the mid-1960's would be $3.45. These U.S. ammonia producers would have gas costs alone of $130 per ton. Total production costs for such producers were $155 to $190 per ton.

Today, PEMEX would have at least a $2.23 per mcf. gas cost advantage ($3.25–$1.02) and a production cost advantage of $84.00 per ton of ammonia compared to a producer purchasing gas in the marketplace today. It would cost PEMEX at most about $15–$20/ton to ship ammonia to the U.S. Gulf ports. PEMEX thus enjoys at least a $65–$70/ton cost advantage over the bulk of U.S. producers in the U.S. ammonia market.

The only real advantage is the cost of gas. Most U.S., Mexican and Soviet plants were built in the last few years, and are modern and efficient.

These production cost advantages are approximate and only illustrate the order of magnitude of the problem. Two-tier pricing clearly gives these foreign producers an enormous production cost advantage. The clear question before the Committee is whether this advantage is created by government subsidies that should be countervailed or whether this is a natural comparative advantage.

The answer is equally clear. This advantage represents a subsidy of exports for a specific group of industries—energy intensive industries like petrochemicals. It does not represent natural comparative advantage.

If Mexico were exercising a comparative advantage on natural gas in the marketplace based on excess supplies and low gas production costs, they would be making it "generally available" to all buyers at basically the same wellhead price (net of transportation to point of use). They also would not be flaring gas; they would be selling it. It would cost PEMEX little to upgrade the capacity of their pipeline to the U.S. border to deliver all the gas they are now flaring, which was 638 million cubic feet per day in 1982. If they sold their flared gas to the United States even at $2.50 at the wellhead, Mexico would earn $1,595,000 per day or $582,175,000 per year.

If PEMEX was exercising comparative advantage, why would they sell to one customer—such as a Mexican customer—at a much lower price when they can sell to another customer—such as a U.S. customer—at a higher price if they wanted to get the most for their gas. But that is what they are doing and flaring gas to boot for a zero return. The Mexican Government simply intervenes in the market and decides prices for gas sales based on the artificial distinction of whether the customer is a Mexican or U.S. customer. Mexico may have political reasons why they want to do that. But such a government policy does not make sense on economic grounds, does not represent sales based on comparative advantage, and costs Mexico an enormous amount of money—much more than they can ever make selling ammonia.

The opponents of this legislation try to make the case that Mexico needs exports to pay their debts to U.S. banks. Then why are they selling ammonia for less than they could in U.S. markets, and why are they flaring gas instead of selling it to U.S. customers at a much higher price than their lower tier domestic price? Certainly not because they are trying to make as much on their energy resources as they can.

Look at two-tier pricing in a slightly different way. What if PEMEX sold all of its gas to anyone, including U.S. customers, at the best price the market would bring? Everyone would pay basically the same wellhead price—domestic customers and U.S. customers. PEMEX can do that because it has a real export market to the United States available by pipeline at a competitive cost. Assume that price is $2.50 per mcf. (or the equivalent in pesos). Suppose PEMEX deducts its costs and pays the difference to the Treasury, and the Mexican Government then writes a check for an amount equal to $1.50 per mcf. (225 pesos per mcf.) to each Mexican industrial gas customer to reduce their net cost to $1.00. Isn't that a subsidy?

If you follow the decisions of the Commerce Department in the countervailing duty cases literally, that would not be a countervailable subsidy because the government writes checks to all Mexican gas customers. That doesn't make any sense. If U.S. law would decide that rebate checks are a subsidy and two-tier pricing is not, that makes even less sense. Such a ruling would mean that a countervailable government subsidy is conferred if it lowers the relative price to domestic producers—rebates—but not if it raises the relative price to U.S. producers through two-tier pricing of the gas input.

I understand the Commerce Department's concern that a general availability standard is necessary to cover traditional and general government services and economic programs like tax policies, public education and construction of roads and the like. As a businessman, I see a big difference between the government selling gas at different prices to favor their own producers and governments deciding how all businesses are generally going to be taxed on profits or capital gains on investments. This is even more true when the government itself gets into the oil and gas or petrochemical business as a direct producer. The government then has engaged in a business. It is not providing a government service in the ordinary sense.

Also, the Committee proposal would limit the application of this upstream subsides amendment to those industries where the subsidized input, like natual gas, constituted a significant portion of the cost of production. The real advantage then is directed to energy intensive industries in the case of gas or fuel oil. In that way, the benefit is conferred on a specific group of industries—energy intensive industries or natural resource based industries, where the raw material input is a significant production cost factor.

In summary on the subsidies issue, certain foreign producers have a huge cost advantage in the production of ammonia. It is one that cannot be matched on commercial terms in current free markets. They have the advantage only because gas as an ammonia feedstock is given to them cheaply. That gas is cheap not because the market has said so, but only because the government says so. But that government gives that special low price only to domestic industries—and requires competitors in free markets to pay a higher export price.

There are two different kinds of ammonia producers competing for all the incremental sales in the U.S. market: those that have their production costs set by the market and those that are given a discriminatory advantage on their production costs directly by their government. They deny their U.S. competitors access to the same low gas price and cost advantage. To top it off, Mexico places a 100 percent tariff on imports of ammonia into Mexico. How protectionist can another country be? How unfair does a government have to be before we call a subsidy a subsidy?

It is even worse in the case of the Soviet Union and Mexico as far as the production and export of ammonia and basic petrochemicals are concerned. Those governments are also the ammonia producers and exporters. They are selling that lower priced government gas to their own petrochemical monopoly.

The proposed amendment only applies where a government has specifically discriminated on the price of raw materials or natural resources between its own producers and the price charged to other producers on export of the same raw material. It does not cover the situation where the government sets a very low price for a raw material, but does not export it. Problems arise if that government then restricts access or discriminates between domestic and foreign producers in that country, but those issues are not being addressed here.

WHY NATURAL RESOURCE SUBSIDIES VIOLATE THE GATT

The objection has been heard that this proposal would somehow conflict with the obligations of the United States under the General Agreement on Tariffs and Trade and/or the Subsidies Code, which interprets that agreement. Such an objection is completely without merit. It is well established that a government may impose countervailing duties on subsidized imports which cause injury to a domestic injury. It is also well established that subsidies may be paid in kind as well as cash by governments to private producers. Nowhere do the GATT, the Subsidies Code or, indeed, the U.S. countervailing duty statute undertake to define the concept of subsidization. The term subsidy is undefined and left to the practice of governments and to the international dispute settlement process.

The sole prerequisites to the imposition of countervailing duties are set forth in Article VI of the GATT and Article IV, V and VI of the Subsidies Code. Nowhere in those articles is there a provision with which this legislation would conflict. Indeed, as evidence that the GATT and the Subsidies Code both contemplate that governments might grant subsidies in the form of goods to domestic producers and thereby distort trade and cause injury, I offer as an example, paragraph (d) of the Illustrative List of Export Subsidies contained in the Subsidies Code:

"(d) The delivery by governments or their agencies of imported or domestic products or services for use in the production of exported goods, on terms or conditions more favourable than for delivery of like or directly competitive products or services for use on the production of goods for domestic consumption, if (in the case of products) such terms or conditions are more favourable than those commercially available on world markets to its exporters."

This language, which is designed to impose on obligation not to grant export subsidies on governments providing inputs to production in the form of goods on terms more favorable than inputs on the production of goods destined for domestic consumption, clearly demonstrates that the Subsidies Code and the GATT itself contemplate that these types of practices can distort trade. The Mexican two-tier price system is, of course, different. But is it really? It may not be an export subsidy, but it is certainly a subsidy on ammonia exports.

In our view, the practices which conflict with international obligations are the subsidies themselves and not the counter-measures. The international obligations that are being breached are the international obligations of the subsidizing governments. The rights of the United States under the international agreements to take countervailing measures against practices of these types, which cause material injury to a domestic industry, are well-settled.

WHY NATURAL RESOURCE SUBSIDIES HARM U.S. INDUSTRIES

An objection has been raised that this proposal deals with an injury which is insubstantial or is caused principally by competition among U.S. producers. This objection misapprehends the return of competition in petrochemical markets and the investment decision cycle in our free market economy.

Foreign petrochemical producers benefiting from subsidized energy resources have a market impact substantially out of proportion to their currently limited share of total U.S. sales. Petrochemicals are sold on a strict price basis in a bid-ask auction market. Because petrochemical demand is independently dictated by the downstream use requirements rather than the current price and is not price elastic (e.g., ammonia demand is largely a function of the price of corn, acres planted and weather conditions), a new seller in the market may trigger a sharp decline in market prices.

The new seller must sell, or offer to sell, at a price below the existing market to get customers. Existing sellers, however, will meet reduced prices to keep their customers. Unless new customers come forward as prices fall, prices will continue to fall until some seller decides to exit the market. Where a new seller of petrochemicals has the advantage of a government-subsidized two-tier price, and the obligation under government-approved development plans to export a substantial quantity in a steady stream, it will simply push the price down until one or more U.S. producers give way. Because all other U.S. producers will be forced to match the exit level price, it may appear that U.S. competition is depressing the price level. Given the information uncertainties of a fast moving bid-ask market, it may even be possible to find situations where U.S. producers appear to have initiated a price cut. Nevertheless, it is clear the root cause of price deterioration is the fixed penetration goal of the subsidized foreign producer who can readily withstand depressed prices.

Experience in the U.S. ammonia market confirms this analysis and shows how the forced exit process works. As subsidized Soviet and Mexican ammonia producers entered the U.S. market, demand remained a function of crop conditions and U.S. producers began to drop out. The first casualties were producers who could divert their natural gas supplies from ammonia production to markets not affected by subsidized competition. To these producers, an ammonia price which did not permit full recovery of market prices for natural gas was tolerable only while the losses arising from shutting down ammonia facilities exceeded the loss of gas value in ammonia sales. As prices dropped, gas value losses became greater than investment losses and the plants were closed.

U.S. producers required to purchase natural gas at full current market prices were also extremely vulnerable as import pressure pushed ammonia prices below the raw material cost of gas alone. For example, a U.S. producer paying even a below-market price of $3.25 per mcf. of natural gas would need a price of $121.88 per ton of ammonia to recover gas costs alone. Such a producer could simply not live in a market where Mexican producers experiencing gas costs of less than $20 per ton of ammonia had pushed Gulf Coast market prices to $120 per ton. Thus, as "take or pay" gas obligations were satisfied, these producers also began to leave the market.

Certain U.S. producers are better able to withstand import pressure in the short run because they have the benefit of long-term arm's length contracts negotiated in a non-regulated gas market in the early 1960's. These contracts, however, are expiring rapidly and will provide only eight percent of domestic gas supplies by 1985 and only less than one percent in 1987. In addition, these contracts are not always sufficient in volume to supply an entire domestic facility and, thus, may be blended into an average price far higher than the subsidized price available to import competitors.

While contract gas supplies may keep some U.S. producers alive until 1987, they provide no basis for the continued investments and gas commitments required to keep the U.S. industry alive in the future. To make an investment in new plant or embark on a major overhaul, a U.S. private investor must be able to anticipate reasonable profits from future operations. To make a commitment for future gas supplies, U.S. producers must reliably expect prices in excess of gas costs. So long as two-tier subsidy practices targeting the U.S. market go unchecked, however, neither reasonable profits nor even full gas cost recovery can be anticipated. Thus, as would be expected, new ammonia plants are not being built in the United States, old plants are not being modernized, and new gas commitments for existing, efficient worldscale plants are not being undertaken.

To put it briefly, two-tiered pricing is both currently injurious and industrially carcinogenic. What is true of ammonia today will be true of other basic petrochemicals tomorrow. To wait until the plant gates actually shut before taking action would be to attack the two-tier disease only when it had become incurable.

HOW TO MEASURE THE LEVEL OF SUBSIDY

We want to turn to a few brief comments on how to measure the level of subsidy. The best standard is one which uses actual prices negotiated at arms' length in today's market between a willing buyer and a willing seller. That is a classic definition of fair market value.

We believe that was the general intent of H.R. 4015, introduced by Rep. Henson Moore, which sets the measure at "fair market value." We understand that the intent of H.R. 4015 is to require the Commerce Department to calculate that price at which Mexican gas or fuel oil, for example, would sell in a free market in an arm's length transaction between a willing buyer and a willing seller.

The task of calculating fair market value of Mexican gas in this example is not impossible. We believe it can be closely approximated in the real world. Look for the most representative prices being currently negotiated in either market (U.S. or Mexico) to be used for current consumption, which is the result of an arm's length transaction between a willing buyer and a willing seller, net of transportation from the wellhead (approximately 90¢–94¢ for Mexican gas to the U.S. border).

Recently a price of $3.10/mcf. was negotiated with Oklahoma Natural Gas Co. by Oklahoma ammonia producers. Currently, intrastate gas in Louisiana is selling for around $3.00–$3.25/mcf. Some recent prices are reported in The Fertilizer Institute production cost to be as high as $4.10/mcf. Transcontinental Gas Pipeline Co. has recently announced it will sell spot gas at about $3.00/mcf. (net of transportation) in

November. As we previously noted, the estimated average cost for recently negotiated gas contracts by U.S. ammonia producers is $3.45/mcf. These are the approximate prices that PEMEX would have to compete with if it decided to offer all of its gas to the market at the best price it could get in the market.

If Commerce determined that the price was in this range and assumed PEMEX offered to sell the gas it was flaring to the U.S. market, the price would probably come out near the low end of $3.00–$3.10/mcf. at the U.S. border. Subtracting 90¢/mcf. transportation cost from the wellhead yields a price of at least $2.10–$2.20. This is at least $1.20/mcf. over the current industrial use wellhead price set by the government in Mexico. At 37.5 mcf. per short ton of ammonia, the Mexican gas subsidy would be at least $45.00/ton.

Given our recent experience with the Commerce Department, we can assure the Congress that Commerce will always pick the lowest prices it can find. They should look to representative prices nearest the probable point of sale at the U.S. border—but they probably will not do so.

WHAT WILL HAPPEN WHEN THE UPSTREAM SUBSIDY AMENDMENT BECOMES LAW

The opponents of this legislation are alleging that dire consequences will result if this bill is passed. It appears most of their real concern is directed to the targeted subsidies and nonmarket economy provisions. But they have raised the spectre of retaliation—presumably by the Mexicans or possibly the Soviets—by refusing to buy U.S. grain. They have also raised the possibility of increased fertilizer prices to farmers. We address each of these issues separately. But, first there will be some very positive benefits that flow from this amendment. It can reverse what will be very bad results if this practice is allowed to continue.

TWO-TIER PRICING ENCOURAGES OVERCAPACITY AND PUTS AMMONIA PLANTS IN THE WRONG PLACE

One of the key indicaters of a subsidy is whether the result would occur in the market absent government interference. Clearly, the market would not set two different prices for gas. The market would also not encourage construction of massive excess ammonia capacity in the Soviet Union and Mexico. These countries may have a comparative advantage in gas due to access by pipeline to contiguous markets and supplies excess to their demand. They do not have a comparative advantage in petrochemicals. Ammonia plants are best located close to markets. They are capital intensive, and such capital is scarce for both Mexico and the Soviets. These are high technology plants, expensive to construct and expensive to run. They require highly skilled workers to make them run efficiently. All of these are disadvantages to Mexico and the Soviets.

Ammonia is expensive to store and transport. About half of total annual production is used in the space of a few weeks in the Spring. There is a massive logistics system—supported at cost by U.S. producers—to deliver nitrogen to the farmers when they need it and in the amounts they need. The efficiency of that system is a major asset of our farm sector. Over the long-term, production should be done in the most efficient place. That produces the lowest long-term cost to the consumer—in this case farmers.

In short, an ammonia plant will only be built that far from market if there is an overwhelming cost advantage to offset all the other inefficiencies and increased costs. The overwhelming advantage in Mexico is the subsidized gas cost. The only way the subsidy can work is to keep the export price of gas high, but that results in flaring of gas. It is clear the market would never do what PEMEX is doing in building excess ammonia capacity for export and flaring gas that they refuse to export.

Passage of this amendment should at least keep such wasteful policies from growing. Hopefully, it would encourage both Mexico and Canada, as well as ourselves, to rely more on markets to set energy prices and halt government intervention that distorts energy supply and prices, and distorts trade.

FREES UP GAS SUPPLIES

If Mexico offered all its low cost gas on the market, it would lower the price for everyone and extend the supplies. It would halt flaring of gas. It might delay production of very high cost gas in the United States, but the market would be more predictable than it is today. This amendment creates a substantial inducement to Mexico to sell its oil and gas at its real market value to everyone on the same basis. The major beneficiaries will be the Mexicans.

Most energy economists believe that gas will sell at about 65–70 percent of the price of oil in a free market. If oil sells for $29/bbl., the equivalent BTU price is $4.94/mcf. Seventy percent of $4.94 is $3.45. As previously noted, that is currently the weighted average price for U.S. ammonia producers on recent gas contracts.

If we discourage the kind of distortion, discrimination and government intervention in markets represented by two-tier pricing, everyone seems better off.

Mexico makes more money on its gas, stops flaring and increases its return on its ammonia investment;

Mexico is better able to pay its debts;

U.S. producers recover their costs and stay in business;

U.S. farmers avoid overdependence on foreign sources of nitrogen fertilizer and enjoy the results of continued competition in the fertilizer business;

Gas prices go down or at least do not rise as rapidly. This benefits the farmers with lower long-term costs of fertilizer and assured supplies;

U.S. producers can make long-term decisions on gas supplies and replacement and modernization of plant; and

Generally, capital and effort are invested in that production which is more efficient, and uneconomic shifts of plants and jobs on both sides of the border are avoided or reduced.

FOREIGN POLICY IMPLICATIONS

We appreciate the foreign policy implications of the current economic difficulties Mexico is having, particularly in the payment of its debts. We appreciate the political difficulties Mexico faces in raising its subsidized oil and gas prices in Mexico. This country has recently undergone a much less wrenching political experience in decontrolling oil and gas prices. But, if the Congress allows the current interpretation of our countervailing duty law to stand, it is sanctioning a clear and evident subsidy and unfair discrimination through two-tier energy pricing. The Congress and the Administration are then asking the U.S. ammonia and petrochemical producers to shoulder the whole burden—and all of the economic loss—of such foreign policy decision. The U.S. Government is condoning a distinct trade distorting and unfair trade practice by a foreign government at the expense of a few U.S. industries. That is just as unfair as asking U.S. farmers to shoulder all of the foreign policy losses from the grain embargo against the Soviet Union.

Mexico cannot pay their debts because they borrowed on the assumption that the price of oil would never drop. There is demand elasticity for oil and gas, and OPEC cannot control it all. If the price goes too high, demand drops and vice versa. Even PEMEX's own publications admit they were subsidizing energy prices and now are starting to raise them to encourage conservation—and to cover their debts. We also point out that Mexico is flaring more gas and losing more dollars by refusing to sell gas for less than $4.40 than PEMEX will ever make on ammonia. The Mexican Government also sets the price of nitrogen fertilizer so low in Mexico that it does not even cover their direct production costs, assuming the gas were free. The average price PEMEX receives for all ammonia sales does not even cover its stated cost of production plus any reasonable return on its investment.

All of this is by way of saying that I am sure the State Department and the Treasury Departmemt are concerned about the economic and political stability of Mexico. We are also. They are a major trading partner as well as a neighbor. We have to get along with each other. I am sure the Administration is concerned about Mexico's bank debts. All we ask is do not put that burden on us alone by allowing subsidized exports of a few energy intensive products, when, overall, Mexico is selling those products at a loss. Mexico is selling most of its gas at a loss. Mexico is flaring gas and selling it for nothing rather than sell it to the United States at what the market would bring. Just on lost sales of flared gas at very conservative prices, Mexico is losing $582,175,000 a year.

In addition, we are not asking Mexico not to sell ammonia here. All we ask is they not be allowed to sell it on a subsidized basis, which allows them to undercut the market price and drive prices down to the point most U.S. producers cannot recover their costs.

Just do not lay all of the burden of Mexico's economic problems on us.

We address the question of possible impact of grain sales or retaliation in following sections of our testimony.

WILL THIS AMENDMENT RAISE FERTILIZER PRICES TO FARMERS

The opponents of this amendment have agreed that this will raise fertilizer prices to U.S. farmers. This is probably correct. The U.S. nitrogen industry cannot continue to exist at the price levels which have been induced by subsidized foreign imports.

A price increase to the U.S. farmer has been grossly exaggerated. Today U.S. farmers are paying 18¢–30¢/bushel of corn (8–13 percent of production cost ex land) for nitrogen fertilizer. An increase in price of 10 percent would only increase farmers' costs 2¢–3¢/bushel.

A responsive U.S. industry will continue to supply vital fertilizer, good years and bad, to meet the farmers' seasonal requirements. The American farmer will be assured of the most efficient distribution and storage system in the world which is financed by domestic nitrogen producers. This distribution system stores production from plants which must be operated year-round, transports fertilizer from production point to the field, and has the capability of delivering to the U.S. farmer an entire year's requirement in a time span of 5–6 weeks.

The American farmer is assured of a future supply which will be insulated from the vagaries of world politics.

The American farmer is insulated from possible cartel pricing of foreign nitrogen producers should the U.S. nitrogen industry cease to exist.

In our judgment, the maximum possible increase in fertilizer costs would be 6¢–10¢/bushel of corn. In many ways, this is an insurance premium for American farmers. The cost of this insurance is small compared with the cost penalties which farmers will pay if they must rely on imports instead of domestic production. The experience of the Spring of 1975 is still vivid in the minds of farmers who paid an average of $265 or $445 a short ton 1983 dollars.

U.S. producers will compete over the short term down to their variable costs when demand is weak. Certain foreign producers are increasing their market share during this weak demand period by price undercutting and price suppression. U.S. producers will not keep producing under those conditions.

Subsidized foreign producers, other exporters and low cost U.S. ammonia producers cannot supply the whole market under normal demand conditions today. Thus, as demand increases, the price will rise.

However, the price will rise only enough to cover variable costs in the face of imports from subsidized producers who have no effective cost constraints on sales. Under these conditions, U.S. producers will run their existing plants on existing gas contracts until those plants are depreciated, then shut down. They will not modernize or replace those plants, and imports will take an increasing market share.

When those imports control the market, imports will no longer be cheap. The price will rise, and U.S. farmers will be dependent on imports.

In addition, many U.S. ammonia producers maintain what amounts to a huge logistical, transportation, storage and marketing system at cost to deliver nitrogen fertilizer to farmers when they need it for planting in the spring and the fall. U.S. producers have relied on profits earned in manufacturing to offset unrecovered logistical costs and yield a return on investment. If U.S. producers can no longer rely on manufacturing profits due to depressed prices or the shut down of production, then the foreign producers or importers will have to pick up the costs and return on the logistical system. Otherwise, the ammonia will not be imported, and the U.S. farmer will not be served. The reliability of delivery will go down. You cannot expect the resellers of ammonia and urea to subsidize these foreign producers by investing in and maintaining the world's most extensive fertilizer distribution of this system.

COUNTERVAILING IMPORT DUTIES AS A THREAT TO U.S. GRAIN EXPORTS

Fear has been expressed that countervailing U.S. import duties, levied to offset upstream foreign subsidies on natural resources, would encourage trade reprisals, and adversely affect U.S. grain exports. The likelihood of such reprisals is debatable, due to the importance of food to the importing countries involved and, in the case of Mexico, the fact that purchase from sources other than the U.S. would materially increase associated shipping costs and result in the loss of credit guarantees provided by the United States.

However, even should such reprisals be imposed, past evidence suggests that their net effect would be limited, since:

1. Countries cutting off U.S. grain exports would be unlikely to discontinue grain purchases. More likely, they would continue to import grain, but shift their purchases to sources other than the U.S.
2. The U.S. tends to serve as a residual supplier to the world in grain trade. Purchases shifted from the U.S. to other countries, therefore, would effectively open alternate markets to U.S. grain and minimize the impact upon U.S. exports.

Support for this latter view is provided by recent statistics for grain trade. For example, U.S. coarse grain export volumes and inventories have varied as follows relative to major competition:

U.S. Coarse Grain Exports
Relative to Other
Major Exporting Nations(a)
(Million Metric Tons)

		(1)	(2)	(3)	(4)	
		Coarse Grain Exports(b)		Ending Coarse Grain Inventories		
Line No.	Grain Marketing Years	U.S.	Other Major Exporters(c)	U.S.	Other Major Exporters(c)	
(1)	1979/80	71.4	27.4	52.7	9.7	11±1
(2)	1980/81	69.5	36.4	34.7	12.1	
(3)	1981/82	58.6	36.1	71.2	9.9	
(4)	1982/83	53.4	27.3	106.1	11.9	
		Increase/(Decrease) From Prior Year				
(5)	1980/81	(1.9)	9.0	(18.0)	2.4	
(6)	1981/82	(10.9)	(0.3)	36.5	(2.2)	
(7)	1982/83	(5.2)	(8.8)	34.9	2.0	

(a) Source of data - U.S. Department of Agriculture.

(b) Exports of corn, sorghum, barley, oats, rye, and millet.

(c) Argentina, Australia, Canada, France, South Africa, Thailand.

As shown by the preceding table, U.S. coarse grain inventories in the past four years have fluctuated year-to-year by as much as 36.5 million metric tons, or 105 percent. The inventory position of major competing exporters, on the other hand, has varied by no more than 2.4 million metric tons, or 25 percent. In effect, the major countries competing with the U.S. in world coarse grain trade have adjusted their export sales to match production and maintained an aggregate coarse grain inventory of about 11 million metric tons, plus or minus one million metric tons. The U.S., in contrast, has occupied the position of residual supplier. Its exports and inventories have fluctuated to the extent necessary to maintain a balance between world supply and demand.

The statistics suggest that foreign production can be expected to be marketed, regardless of the U.S. export position, i.e., with or without trade sanctions. The maximum U.S. vulnerability to cutoff of coarse grain imports due to trade reprisals, therefore, can be estimated to amount to no more than about 2.0–2.5 million metric tons, the typical year-to-year swing in coarse grain inventories held by competing exporting nations. This equates to about 3 percent–5 percent of U.S. coarse grain trade. Any greater shift of business from the U.S. to alternate suppliers could be expected to open substitute markets for U.S. grain, and, over a period of several years, the U.S. vulnerability could be expected to approach zero, as foreign inventories were depleted.

Practical evidence of market shifting is provided by the relatively small change which occurred in U.S. coarse grain exports between the 1979/80 and 1980/81 marketing years. In 1980, the U.S. embargoed grain sales to the Soviet Union, and, as a result, U.S. coarse grain exports to the USSR fell by 6.3 million metric tons, or 56 percent. Soviet imports of coarse grains from sources other than the U.S., however, rose by an offsetting 6.0 million metric tons, and total U.S. coarse grain exports were reduced by only 1.9 million metric tons, or 2.7 percent, as U.S. exports were shifted to markets opened as the result of shipments by other suppliers to the USSR.

A similar relationship between the U.S. and its competitors is evident in the export statistics for wheat:

U.S. Wheat Exports
Relative to Other
Major Exporting Nations(a)
(Million Metric Tons)

		(1)	(2)	(3)	(4)	
		Wheat Exports		Ending Wheat Inventories		
Line No.	Grain Marketing Years	U.S.	Other Major Exporters(b)	U.S.	Other Major Exporters(b)	
(1)	1979/80	37.4	44.4	24.5	17.9	
(2)	1980/81	41.2	43.1	26.9	13.5	16±2
(3)	1981/82	48.3	47.4	31.7	15.0	
(4)	1982/83	41.1	50.9	41.9	17.1	
		Increase/(Decrease) From Prior Year				
(5)	1980/81	3.8	(1.3)	2.4	(4.4)	
(6)	1981/82	7.1	4.3	4.8	1.5	
(7)	1982/83	(7.2)	3.5	10.2	2.1	

(a) Source of data - U.S. Department of Agriculture.

(b) Argentina, Australia, Canada, France.

During the past four years, U.S. inventories of wheat have fluctuated year-to-year by up to 10.2 million metric tons, or 32 percent. Inventories held by other major exporting countries, on the other hand, have varied a maximum of 4.4 million metric tons, or 25 percent. Effectively, the major foreign exporters have held their carry-over inventories of wheat at about 16 million metric tons, plus or minus two million metric tons, by matching exports to production. U.S. exports and inventories, in contrast, have swung to the extent required to maintain an overall world balance. The statistics suggest a maximum (single year) U.S. vulnerability to trade reprisals of about 4.0-4.5 million metric tons, or roughly 8 percent-12 percent of U.S. wheat trade. As in the case of coarse grains, this vulnerability could be expected to decline with time, and likely approach zero after several years.

The principle of market shifting is also evident in the statistics for wheat exports. Between the 1979/80 and 1980/81 marketing years, U.S. exports of wheat to the Soviet Union declined by 0.9 million metric tons, or 23 percent, as the result of the U.S. grain embargo. During the same period of time, Soviet purchases of wheat from other countries increased by 4.8 million metric tons, or 59 percent, but this was almost precisely offset by an increase of 4.7 million metric tons in U.S. wheat exports to the balance of the world. In net, the overall volume of U.S. wheat trade was not materially affected by the loss of Soviet business.

Chairman GIBBONS. Thank you.

Our next witness is from the California Portland Cement Co., Mr. Gerstell.

STATEMENT OF A. FREDERICK GERSTELL, PRESIDENT AND CHIEF OPERATING OFFICER, CALIFORNIA PORTLAND CEMENT CO., ON BEHALF OF COALITION OF U.S. CEMENT PRODUCERS AND WORKERS

Mr. GERSTELL. Good morning, Chairman Gibbons and members of the committee, it takes a lot to get a Californian out of his home State, particularly on a rainy day in Washington, but the importance of the agenda this morning and the leadership of a Floridian did the trick for us. I am Fred Gerstell, president and chief operating officer of the California Portland Cement Co., the largest producer of cement in southern California and Arizona.

I address you today on behalf of a coalition of cement unions and domestic producers with plants in 12 States. We seek your support for a change in the countervailing duty law, so that we can compete with the rapidly increasing volumes of Mexican cement entering our markets.

Cement making is a highly energy intensive—from electric power needed to run the grinding mills, to the fossil fuel needed to burn kilns at 2,800° F. Mexico has built enormous new cement plants and expanded existing ones. The Mexican plants operate with energy supplies virtually free by Pemex, the Government oil monopoly, under Mexico's two-tier energy pricing system. Cement from these plants is now flowing at accelerating rates into U.S. markets, from San Diego to Tucson, El Paso to Houston, and across to Miami. As my full testimony shows, Mexican imports have soared sixfold in the last year.

Virtually none of this cement would be sold in the United States if the Mexican plants were not given the Government-controlled, bottom-tier price on fuels. Because this cheap oil erases almost half of their production costs, the Mexican plants have been able to undersell U.S. producers virtually anywhere they can reach by ship, truck or rail.

The domestic cement industry has no fear of competition. We welcome it. The coalition I speak for represents some of the most technologically advanced production in the world. This point is important: Unlike other industries, we do not ask to be rescued from a failure to modernize our plants. Our modern plants match any worldwide, including Mexico's.

But, even with the most advanced technology, we cannot compete against imports produced with virtually no-cost, Government-supplied energy. The benefit conferred on Mexican plants by the two-tier Pemex price skews the competition unfairly. It must be made countervailable—now, before the damage to our domestic industry becomes irrepairable.

Many domestic producers have postponed or cancelled vital capital improvements because of the damage and uncertainty from imports. Let me illustrate. Our facility near Tucson has both a new plant and an older one. We must decide soon whether to modernize the older plant, build a new one, or shut it down entirely. If we are forced to shut the plant down because of the rapid increase of Mexican imports, many jobs will be lost. And a major region of the country will be left dependent on foreign cement for a large part of its supply—from a source that has no commitment to the region.

New Mexican cement plants, with a large surplus capacity designed for export, receive fuel oil from Pemex at approximately $1.23 per barrel. That same oil is priced for export by Pemex at roughly $27 per barrel, 20 times the price to the Mexican plants.

Defenders of the Mexican Government's two-tier pricing say that the 2,000-percent differential for fuel oil between the export price and the industrial user price reflects some natural cost advantage. From my perspective, there is nothing natural about it at all. It distorts free trade.

While the subcommittee is considering three options, we believe the best approach is the export price formula. But all three options share the right general objective—to measure the subsidy by the legitimate market value of the benefit. The amendment will apply only where the input represents a significant portion of production cost, and it is imperative that the subcommittee choose a formula that measures the real commercial value of the controlled input price to the exporting firm.

The production cost of the input is an inappropriate test for three reasons: First, it has nothing to do with the fair value of energy inputs in internationally competitive markets. What it cost Pemex to produce the fuel it supplies to Mexican producers tell us nothing about what our Mexican competitors would have to pay—if the Government did not relieve them of almost all of this essential cost element.

Second, an analysis of production costs for Government-owned energy supplies would be unworkable.

Finally, the Commerce Department's usual practice is to rely on the market value of the benefit passed to the foreign producer not just the mere cost of production.

In sum: By relieving its cement manufacturers of energy costs, Mexico is setting the stage for them to strangle the U.S. producers. Our current countervailing duty law is ineffective against this unfair practice. We need an energy input amendment, with a realistic market value standard for measuring the subsidy.

Mr. Chairman, I have a full statement which I would like to submit for the record at the proper time.

[The prepared statement follows:]

STATEMENT OF A. FREDERICK GERSTELL, PRESIDENT AND CHIEF OPERATING OFFICER, CALIFORNIA PORTLAND CEMENT CO., ON BEHALF OF COALITION OF U.S. CEMENT PRODUCERS AND WORKERS

Chairman Gibbons and members of the subcommittee, I am Fred Gerstell, President and Chief Operating Office of California Portland Cement Company, the largest producer of cement in Southern California and Arizona. I address you today on behalf of a coalition of cement unions and domestic producers with plants in 12 states.[1] As you know, cement producers make cement from crushed rock and sell it to concrete companies, who mix it with water and pout it at construction sites. Our coalition has worked for months to find a means of combating subsidized cement imports from Mexico, and our industry needs this Subcommitee's help now.

Stated bluntly, Mr. Chairman, our industry is braced for a tidal wave that we may be powerless to stop without a change in the countervailing duty law. Mexico has built enormous new cement plants and expanded existing ones. Cement making is highly energy intensive—from electric power need to run the grinding mills, to the fossil fuel needed to burn kilns at 2800°F. The Mexican plants operate with energy supplied virtually free by PEMEX, the government oil monopoly, under Mexico's two-tier energy pricing system. Cement from these plants is now flowing at accelerating rates into U.S. markets, from San Diego to Tucson, El Paso to Houston, and across to Miami. Virtually none of this cement would be sold in the U.S. if the Mexican plants were not given the government-controlled, bottom-tier price on

---

[1] The coalition includes the following companies (with location of plants and facilities): California Portland Cement Company (Mojave and Colton California; Rillito, Arizona). General Portland, Inc. (Tampa and Miami, Florida; Paulding, Ohio; Fredonna, Kansas; Fort Worth, Dallas, and Balcones, Texas; Los Robles, California; Whitehall, Pennsylvania; and Demopolis, Alabama). Gifford-Hill Cement Co. (Crestmore and Oro Grande, California; Clarkdale, Arizona; Midlothian, Texas; Harleysville, South Carolina; Dallas Texas). Kaiser Cement Corporation (Permanente and Lucenrne Valley, California; Waianae, Hawaii; Montana City, Montana; San Antonio, Texas; Oakland, California). Southwestern Portland Cement Co. (Victorville, California; Fairborn, Ohio; and Amarillo, El Paso and Odessa, Texas). Monolith Portland Cement Co (Monolith, California; Laramie Wyoming).

It also includes the United Cement, Lime, Gypsum and Allied Workers International Union, AFL/CIO, CLC (headquartered in Chicago, Illinois), which represents approximately 78 percent of the cement plant production and maintenance workers in the United States.

fuels. Because this cheap oil erases almost half of their production costs, the Mexican plants have been able to undersell U.S. producers virtually anywhere they can reach by ship, truck, or rail.

The cement industry has no fear of fair competition. We welcome it. The coalition I speak for represents some of the most technologically advanced production in the world. Ours is a modern, efficient, innovative industry. We have undertaken major capital investment programs to develop energy efficient production. At California Portland, for example, we have completed a $110 million new plant north of Los Angeles and are presently constructing a $45 million state-of-the-art electric co-generation facility at our Colton, California plant that will enable us to generate our own electrical power. This point is important: unlike other industries, we do not ask to be rescued from a failure to modernize. Our plants match any worldwide, including Mexico's.

But even with the most advanced technology, we cannot compete against imports produced with virtually no-cost, government-supplied energy. The benefit conferred on Mexican plants by the two-tier PEMEX price skews the competition unfairly. It must be made countervailable—now, before the damage it is doing to our domestic industry become irreparable.

Let me briefly summarize why this problem has become so pressing.

RAPID INFLUX OF MEXICAN CEMENT

Within the last several months Mexican imports have increased dramatically in the Southwestern and Gulf states. In late 1982, large volumes of Mexican cement suddenly began to flow into Southern California. A short time later, large shipments suddenly started to Arizona and Florida. Almost no Mexican cement had been sold in these before. Suddenly, imports were soaring—and they have continued to climb. All totaled, Mexcian cement imports into the U.S. multiplied 660 percent in the first 7 months of 1983 over the same period for 1982.[2]

It is clear that this sharp climb will continue. Owners of Mexican companies have recently acquired import terminals in San Diego and Florida. They have purchased cement consumers and distribution terminals in Arizona. These acquisitions illustrate the deadly seriousness of the threat to U.S. producers. They rob our customer base from us. Last year, for example, a major Mexican producer completed a new 1-million-plus ton plant at Hermosillo, 175 miles south of the Arizona border. This plant is so large, and in such as remote and sparsely populated location, that it could have been designed only with substantial exports in mind. Events soon confirmed the plant's export strategy. Soon after the Hermosillo plant began production, its owners bought distribution terminals and ready-mix concrete dealers in Phoenix and Tucson. Remember that ready-mix outlets are our main consumers of cement.

Mexican cement is now moving to those facilities at geometrically expanding rates. In addition, barge shipments have started from Hermosillo to the import terminal at San Diego, California. Using the huge advantage provided by $1-per-barrel oil, the importers sell their cement well below the U.S. market price, dragging prices down swiftly.

This Mexican incursion comes at an unusually vulnerable time for the domestic cement producers. Construction, and therefore cement sales, have been depressed. Domestic producers have operated below 65 percent of capacity for months. In addition, California producers have suffered severely from dumped Australian and Japanese cement imports.[3] Many cement companies have posted losses—for California Portland, the first since the Great Depression. Many have sold valuable assets to raise capital.

In addition, many have postponed or cancelled vital capital improvements because of the damage and uncertainty from imports. Let me illustrate. Our facility near Tucson has a new plant and an older one. We must decide soon whether to modernize the older plant, build a new one, or shut it down entirely. If we are forced to shut the plant down because of the rapid increase of Mexican imports, many jobs will be lost. The area economy will suffer from lost investment and construction work. And a major region of the country will be left dependent on foreign cement for a large part of its supply—from an unreliable source that has no commitment to the region. That's how important this amendment is to our industry.

---

[2] 1983 and 1982 imports from Mexico are shown in Exhibits A and B to this testimony.

[3] Last month the Commerce Department found these imports were being dumped at rates up to 136 percent below their fair value.

THE EFFECT OF THE TWO-TIER PRICE DIFFERENTIAL

The cement manfacturing process basically involves crushing, grinding, and burning rock to make cement. The process is highly energy intensive. In the United States and most other countries, where fuel and power are not subsidized, the cost of energy accounts for nearly 50 percent of direct cement manufacturing costs.

The Mexican government's National Industrial Development Plan declares that its government follows "an explicit policy of maintaining internal prices of energy sources for industrial use below that of the international market. This allows for the strengthening of industry by giving it substantial margin of protection via inputs. In contrast to other forms of protection which tend to make such costs more expensive and access to external markets more difficult, this mechanism constitutes a direct incentive to exports."

Joint government-cement industry Development Plans, building on this goal of increased "access to external markets," have called for construction of surplus new capacity for exports. As a result, plants exporting to California, Arizona, Florida and Texas have expanded dramatically in the last few years—some as much as 12-fold.[4]

These plants receive fuel oil from PEMEX at approximately $1.23 per barrel.[5] The same oil is priced for export by PEMEX at roughly $27 per barrel, more than 20 times the price to the Mexican plant. Translated into actual sales values, the overall benefit to Mexican producers from the energy subsidy is in the range of $20 per ton.

Without this benefit, Mexican producers would be unable to deliver cement economically in U.S. markets at prevailing prices. With the benefit, Mexican producers are able to overcome significant transportation costs and still deliver cement far below the market price.

THE BENEFIT CONFERRED BY TWO-TIER PRICING SHOULD BE COUNTERVAILABLE

Defenders of the Mexican government's two-tier pricing say that the differential for fuel oil between the export price and the industrial user price—a differential that exceeds 2000 percent in Mexico—reflects some natural cost advantage.

From a businessman's perspective, there is nothing natural about it at all. The price is fixed by government monopoly, not by natural economic forces. The price level is explicitly intended to promote uneconomic new expansion—such as cement plants that must attempt to serve unnaturally distant markets hundreds of miles away. It artificially lowers the cost of the primary production element, enabling the foreign manufacturer to remain in distant markets despite other disadvantages.

This can only distort the natural patterns of trade. It seems to me that countervailing is fully justified in these circumstances.

MEASURING THE BENEFIT

The Subcommittee is considering three options for measuring the benefit conferred by the two-tier price subsidy. The best approach is the export price formula, for reasons I will describe in a moment. But all three options appear to share the right general objective—to measure the subsidy by the legitimate market value of the benefit. As long as the test turns on comparisons to real transactional prices—and not on non-market factors such as cost of production—the result should be satisfactory.

The export price formula is the cleanest approach. In most cases, the export price set by the country in question will closely approximate the international market price. It will be easily identifiable, since the two-tier pricing claim will depend on proof that the country maintains separate domestic and export prices. The same price-setting body will have set both prices, export and domestic, for the country. By permitting U.S. import authorities to adopt that differential as the measure of subsidy, the export price formula would avoid complicated administrative calculations and would give the foreign country clear notice of the countervailing response its pricing practice will produce. This would serve the Subcommittee's goal of simplifying the trade laws where possible.

The critical point, simplicity aside, is that the test must provide relief from the unfair competitive advantage bestowed by the government-subsidized energy. The amendment will apply only where the input represents a significant portion of pro-

[4] These capacity expansions are shown as Exhibit C to this testimony.

[5] Prices quoted in this testimony are as of February 1983. Current Mexican export quotes remain in the $27 per barrel range.

duction cost,[6] and it is therefore imperative that the Subcommittee choose a formula that measures the real commercial value of the controlled input price to the exporting firm.

This appears to be the aim of the "fair market value" test (Option Three), originally developed by Congressman Moore. The first two factors of this proposal, the world price and the generally available price of the input to U.S. industrial producers, would yield legitimate market value comparisons. The other two factors would not, and we believe they do not belong in the Subcommittee formula.

Production costs are a particularly inappropriate factor, for three reasons. First, they have nothing to do with the fair value of energy inputs in internationally competitive markets. Current market prices for fuel oil inputs bear no relationship to production costs, which are minimal. In the cement business, where energy costs, are the most important element in overall production, the question is how much a manufacturer must pay to get fuel and power to run the plant. What it costs our supplier to produce the fuel is of no consequence to our business. Similarly, what it cost PEMEX to produce the fuel it supplies to Mexican producers tells us nothing about our Mexican competitors would have to pay if the government did not relieve them of almost all of this essential production component.

Second, calculations of production costs for government-owned energy suppliers abroad would be unmanageably complex. Little reliable information will be available. With all the complexities facing our import officials in administering these laws, it doesn't make sense to ask them to act on a hunch about PEMEX's production costs.

Finally, it would go against the grain of the Commerce Department's own practices to look to production cost rather than to the market value of the benefit passed to the foreign cement producer. I note, for example, that the European Communities argued in the steel cases that the value of preferential loans to European steel producers should be measured by "the financial contribution of the government rather than the much more nebulous benefit to the recipient."[7] The Commerce Department rejected this argument. It applied its long-standing practice of measuring government-provided loans and guarantees against the prevailing commercial rate paid to private lenders.

I see no reason why the practice should be different for subsidized energy inputs. The standard should be the commercial price of fuel oil ir. market transactions. The cost of production is irrelevant.

CONCLUSION

By relieving its cement manufacturers of energy costs, Mexico is setting the stage for them to strangle the U.S. producers. Our current countervailing duty law is ineffective against this unfair practice. We need an energy input amendment, with a realistic market value standard for measuring the subsidy.

[6] As a technical drafting matter, the language should reflect the fact that the input would be a significant portion of the cost of manufacture but for the controls, which will reduce the input's actual significance as the controlled price grows farther from the market price.

[7] "Certain Steel Products From Belgium," 47 Fed. Reg. 39304, 39330 (1982).

U.S. IMPORTS FROM MEXICO OF PORTLAND HYDRAULIC CEMENT, OTHER THAN WHITE NONSTAINING, BY CUSTOMS DISTRICT AND MONTH, 1983.
VOLUME IN SHORT TONS AND CIF VALUE IN U.S. DOLLARS.

1983	14: NORFOLK, VA		18: TAMPA, FL		23: LAREDO, TX		24: EL PASO, TX		25: SAN DIEGO, CA		26: NOGALES AZ		52: MIAMI, FL		U.S. TOTAL	
	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$
JAN	-	-	-	-	6,090	227,136	995	39,481	2,877	153,058	44	1,112	13,064	522,560	23,070	943,347
FEB	-	-	-	-	5,781	206,502	2,154	101,418	5,985	314,143	132	3,336	-	-	14,052	625,399
MAR	26	1,122	-	-	8,013	261,852	4,320	194,143	4,803	318,031	1,056	42,655	6,594	250,572	25,812	1,068,375
APR	-	-	6,772	250,588	7,036	232,184	6,340	277,783	5,824	310,785	2,277	96,912	7,295	277,210	35,544	1,445,462
MAY	-	-	12,267	466,146	7,028	234,487	7,161	330,453	9,791	545,912	5,263	224,310	37,330	1,328,477	78,840	3,129,785
JUNE	-	-	7,909	299,755	7,330	247,507	10,078	445,029	12,389	663,534	5,536	236,041	21,204	754,355	64,446	2,646,221
JULY	-	-	6,119	231,925	6,354	226,775	6,383	289,303	11,193	608,231	2,257	96,114	14,558	551,748	46,864	2,004,096
AUGUST	-	-	13,113	451,515	6,650	230,015	10,967	494,834	7,889	340,713	8,130	346,692	18,369	724,338	65,118	2,588,107
TOTAL	26	1,122	46,180	1,699,929	54,282	1,866,458	48,398	2,172,444	61,751	3,254,407	24,695	1,047,172	118,414	4,409,260	353,746	14,450,792

Source: U.S. Department of Commerce, Bureau of the Census (IM-145X). Data presented is "General - All Methods of Transportation."

U.S. IMPORTS FROM MEXICO OF PORTLAND HYDRAULIC CEMENT, OTHER THAN WHITE NONSTAINING, BY CUSTOMS DISTRICT AND MONTH, 1982.
VOLUME IN SHORT TONS AND CIF VALUE IN U.S. DOLLARS.

1982	23: LAREDO, TX		24: EL PASO, TX		25: SAN DIEGO, CA		26: NOGALES, AZ		18: TAMPA, FL		52: MIAMI, FL		U.S. TOTAL	
	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$	STN	US$	STN:	$:
JAN	3,667	208,409	50	2,882	-	-	80	8,503	-	-	-	-	3,797	219,794
FEB	3,553	195,079	26	1,509	-	-	-	-	-	-	-	-	3,579	196,588
MAR	5,772	339,558	133	8,762	5	325	-	-	-	-	-	-	5,910	348,645
APR	6,739	292,434	192	11,461	-	-	-	-	-	-	-	-	6,931	303,895
MAY	11,087	590,638	25	1,499	-	-	-	-	-	-	-	-	11,112	592,137
JUN	8,390	483,853	215	11,467	45	3,372	-	-	-	-	-	-	8,650	498,692
JUL	5,033	279,367	125	7,485	380	24,917	-	-	-	-	-	-	5,538	311,769
AUG	7,374	327,387	97	7,107	731	46,410	-	-	-	-	-	-	8,202	380,904
SEP	10,655	350,650	98	4,955	1,179	67,844	-	-	-	-	-	-	11,932	423,449
OCT	7,285	268,297	361	21,783	1,820	98,754	-	-	-	-	-	-	9,466	388,834
NOV	7,513	256,332	474	26,032	3,220	173,707	-	-	-	-	-	-	11,207	456,071
DEC	6,059	186,876	383	19,593	7,247	409,097	-	-	6,421	233,000	6,117	244,680	26,227	1,093,246
TOTAL:	83,127	3,778,880	2,179	124,535	14,627	824,426	80	8,503	6,421	233,000	6,117	244,680	112,551	5,214,024

Source: U.S. Department of Commerce, Bureau of the Census (IM-145X). Data presented is "General - All Methods of Transportation."

B

ANNUAL PRODUCTION CAPACITIES OF MEXICAN CEMENT PLANTS
EXPORTING PORTLAND CEMENT AND/OR CEMENT CLINKER
TO THE UNITED STATES, IN THOUSANDS OF SHORT TONS,
1973 TO 1982.

Cement Company/Plant	1973	1974	1975	1976	1977	1978	1979	1980	1981	1982
Cementos Anahauc/Tamuin	660	660	1749	1749	1749	1749	1749	1749	2409	2846
Cementos de Chihuahua/ Chihuahua	-	-	-	-	-	-	-	-	-	660
Cementos de Chihuahua/ Ciudad Juarez	116	116	116	116	116	132	132	132	160	206
Cementos Hidalgo/ Hidalgo	264	264	264	248	253	468	578	578	578	625
Cementos Mexicanos/ Ensenada	190	190	190	190	190	190	586	627	792	990
Cementos Mexicanos/ Monterrey	990	1386	1386	1254	1254	1700	1700	1700	2492	2620
Cementos Tolteca/ Hermosillo	112	112	112	112	112	112	112	109	1100	1427

Sources: The Mexican Economy and Cement Industry, Portland Cement Association (1981), Ex. 4; Anuario 1981, Camara Nacional del Cemento; Map: Portland Cement Plants, U.S., Canada & Mexico, Pit and Quarry Publications, Inc. (1982); and Kaiser Cement Corporation.

Chairman GIBBONS. It will all be included. Statements of all the witnesses today will be included in the record as if delivered.

Mr. Bronson, before we go to you I want to pause a moment and recognize Mr. Hance and then Mr. Jones.

Mr. Hance.

Mr. HANCE. Thank you, Mr. Chairman.

I would like at this time to welcome from the lower Rio Grande Valley of Texas, Mr. John McCoy and Mr. Tony Cordova. Mr. McCoy will be testifying. He is the owner of Valley Brick & Block. His business is on the U.S. side of the Mexican border and when a shot is fired across the border, he is the first to get hit. I appreciate his being here to tell us about his firsthand experience with this problem.

Also, Mr. Chairman, I have two short statements I would like to make a matter of record. One is a description the staff did on the Mexican program. The other is a letter from the United Cement, Gypsum, and Allied Workers Union on this matter.

Chairman GIBBONS. We will place them in the record.

[The information follows:]

THE MEXICAN CEMENT INDUSTRY DEVELOPMENT PROGRAM

The Mexican cement industry has grown rapidly in recent years, with the aid of the active intervention of the Mexican Government. This aid and encouragement has taken the form of a specific "Development Program For The Cement Industry," published by the Mexican Government in 1980.

The cement industry plan sets minimum goals for additions to Mexican cement production capacity in the period 1980–1983, which amount to an aggregate increase of approximately 77 percent. A substantial amount of this new capacity has been added to areas bordering on the United States, in areas with inadequate domestic demand to warrant the new or expanded plants. The cement industry plan also provides for a variety of specific government assistance, including: a 20 percent tax credit on installed capacity expansion, a tax credit for new employment, a five percent tax credit for the purchase of Mexican-origin equipment, special immediate depreciation of machinery and equipment, and permission to transfer certain tax benefits among related companies. In addition, the cement industry plan provides for domestic cement price controls and sets cement export targets.

This plan is an adjunct of the Mexican Government's National Industrial Development Plan, which outlines the national strategy for industrial development and lists the Mexican cement industry as a "priority industry," entitled to the highest level of government encouragement and benefits. The National Industrial Development Plan states that the Mexican Government "adopts as an explicit policy the principle of maintaining, at a lower level than the international one, the domestic price of industrially-used energy sources and basic petrochemicals."

It adds that this policy has among its objectives "the promotion of exports and the efficient substitution of imports."

The special advantages that this policy confers upon the Mexican cement industry is expressly acknowledged in the Cement Industry Development Plan, which states that "the manufacture of cement is an excellent option for the increased-value conversion of energy sources."

That is to say, the Mexican Government has adopted the policy of leveraging its natural comparative advantage on petroleum and petroleum products into an artificial advantage in certain energy-intensive products such as cement, bestowed through the intervention of the government in the market.

Exhibit 2

(TRANSLATION)

Remittance No. 6 1-VII-80/1

DEVELOPMENT PROGRAM FOR THE CEMENT INDUSTRY

[Published in the "Diario Oficial" (Official Journal) of the Federation, July 1, 1980]

In the margin, a seal with the National Escutcheon, which reads: Estados Unidos Mexicanos.-Secretaría de Patrimonio y Fomento Industrial (United States of Mexico - Department of Patrimony and Industrial Development).

DAVID IBARRA MUÑOZ, JOSE ANDRES OTEYZA and JORGE DE LA VEGA DOMINGUEZ, Secretary of Finance and Public Credit, Secretary of Patrimony and Industrial Development, and Secretary of Commerce, respectively, pursuant to the provisions of Articles 31, Section IV; 33, Section XII; and 34, Section VI of the Organic Law of the Federal Public Administration, and Articles 16 of the Revenue Law of the Federation for Fiscal Year 1980; 30 of the Tax Code of the Federation; 6, 7, 20, 21 and 22 of the Decree providing for Implementation of the National Industrial Development Plan and establishing the Bases of Coordination for its execution; 11 and 17 of the Decree establishing Tax Incentives for the Development of Employment and investment in Industrial Activities; 6 and 9 of the Decree granting Price Differentials on Energy Sources and Basic Petrochemical Products to Firms which build New Industrial Plants, published in the "Diario Oficial" of the Federation on December 29, 1978, amended by a subsequent Decree published in the "Diario Oficial" on June 19, 1979; hereby issue the following:

(See the Decrees cited, pages 19-III-79, 6-III-79 and 29-XII-78, respectively, in the Industrial Decentralization Section)

DEVELOPMENT PROGRAM FOR THE CEMENT INDUSTRY

CHAPTER I

Background

In the framework of the Alliance for Production, the Cement Industry signed a Coordination of Action agreement in December 1976, whereby it agreed to guarantee the national and regional supply of cement in the 1977-1982 period and to generate a surplus for a substantial increase in exports in this sector, which involved "increasing current production by 8 million tons, 2 million tons of which will be exported". This represented an 8% average annual increase in supply.

The federal government accorded the cement industry a 15% price increase in May 1978 and agreed to a 75% subsidy on the importation of machinery and the application of accelerated depreciation. This assistance was granted for the purpose of strengthening reinvestment capabilities with domestic sources of income, thereby consolidating the required expansion.

Based on the prevailing economic conditions in 1976 and the six-year growth projections, the industry's commitment was sufficient both to satisfy domestic demand and to export. Upon reviewing these projections at the end of 1978, and on the basis of the information and objectives of the National Industrial Development Plan, the results were substantially modified since the growth of the construction industry was greater than expected, creating problems in cement supplies, a situation which became critical in 1979.

The abovementioned problems necessitated the formulation of a new investment program and the intensive promotion of new project generation. In this context, and taking into account the fact that the manufacture of cement is an excellent option for the increased-value conversion of energy sources and the utilization of the non-metallic mineral resources of the country, and, in addition, contributes indirectly to the large-scale creation of employment, the National Industrial Development Plan accords the cement industry the maximum tax incentives established by the Plan.

In 1979 this Department, in conjunction with other Executive agencies and the industrial sector, after various work meetings, devised a new investment program calling for an increase in annual production for the 1980-1983 period of 13.1 million tons, with an approximate investment of 35 billion pesos. This represents a 64% increase over the original commitment.

The abovementioned tax incentives notwithstanding, it was decided, in order to ensure realization of the necessary investments, to grant the cement industry several additional incentives for the purpose of obtaining greater financial resources for reinvestment.

CHAPTER II

Goals

In accordance with the goals of the National Industrial Development Plan and on the basis of the planning effort made in conjunction with the productive sector, it is estimated that the national demand for cement will grow at an average annual rate of 11-12% during the 1979-1982 period and 13.5-14.5% from 1983 to 1990.

Given the highly competitive price and quality of Mexican cement and the increasing demand for this product in both the domestic and the international markets, this industry should grow during the 1980-1983 period in the following manner:

Year	1980	1981	1982	1983
% Additional capacity	7.97	31.22	17.80	14.43
Total Capacity in Dec. (thousands of tons)	18,032	23,662	27,875	31,900
Estimated Production (thousands of tons)	17,564	20,366	24,512	28,847

The above accounts for adequately supplying the national market and expanding the productive base to export 10% of production.

However, increased imports of certain special types of cement not manufactured in the country are foreseen; nevertheless, the value of such imports will be significantly smaller than that of exports.

The geographic location aspect of the industrial development policy is intended to channel new investment in cement production into regions with characteristics favorable to its development, as a function of its national as well as its regional impact. Thus, it is suggested that the cement industry, as a high-volume user of energy sources, be located in areas that are considered to have high-priority in the National Industrial Development Plan and that have an existing or anticipated supply of natural gas. Being a Category 1 activity, it will also be promoted in other areas, provided that its production is linked industrially and geographically to the use of limestone. This will also result in a more efficient regional supply.

CHAPTER III

Federal Government Assistance

To achieve the objectives set forth in the National Industrial Development Plan and the specific goals of this Development Program, the Federal Government will provide the following assistance:

1. The manufacture of cement has been classified in Category 1 as a strategic industrial sector input, pursuant to the Resolution of March 9, 1979, and will consequently be entitled, depending on its geographic location in accordance with the Decree of February 2, 1979, to the following incentives for new industrial plants generated in this sector:

(See the Resolution and the Decree cited, pages 9-III-79 and 2-II-79, respectively, of the Industrial Decentralization Section)

- 20% Tax Credit for new investments or installed capacity expansion anywhere in the national territory except Zone III A. In Zone III B, expansions up to 100% only, on a one-time basis.

- Tax Credit for the generation of new employment, equivalent to 20% of the annual general minimum salary in the corresponding economic zone, multiplied by the number of additional jobs generated, which must be kept open for a minimum period of two years under the terms of the Decree of March 6, 1979.

(See this Decree on page 6-III-79 of the Industrial Decentralization Section)

- 5% Tax Credit on the purchase value of new national production machinery and equipment pursuant to the Decree of March 6, 1979.

- Price Differentials on the consumption of energy sources up to 30% of the corresponding billing at current national prices, if located in Zone I A; or 10% on fuel oil or 15% on gas if located in Zone I B, pursuant to the Decrees of December 29, 1978 and June 19, 1979. In both zones they will be (deducted) from payment of the electrical energy contract amount for new plants.

(See the regions comprising Zone I and the Decree cited, pages 2-II-79 and 29-XII-78, respectively, of the Industrial Decentralization Section)

II. In addition, the following incentives will be granted:

- Taking into account the fact that the construction period for a cement plant is approximately 3 years and that during this time the firm does not incur sufficient tax obligations to fully benefit from these incentives, Tax Promotion Certificates may be used by other firms belonging to the same investment group as the beneficiary which are also involved in the production of cement.

- Depreciation of machinery and equipment, beginning on the date of issuance of the Tax Promotion Certificate for the property being depreciated.

- Two price levels will be established: F.O.B. Plant and the maximum price to the public delivered to the work site: this price shall be applicable to purchases of 5 or more tons. For smaller purchases, the prices shall be on the basis of delivery to the distributor's warehouse. The F.O.B. Plant price shall be determined on the basis of the four regions where the cement producing plants are located. The maximum price to the public shall be included in the regional F.O.B. Plant price, plus charges for freight, handling and the distributor's profit margin. When plants make direct sales to the end-user, delivered to the work site, the corresponding maximum price to the public may be charged. Direct sales to public sector agencies and institutions shall be billed using the F.O.B. Plant price and, in those instances where the cement is delivered to the work site, corresponding freight and handling charges may be added; in both cases existing preferential margins shall be applied. To fully implement the industry's investment program, a surplus cement supply will be produced in 1981, permitting (?)regulation of market prices.

- Pursuant to the guidelines issued by the Department of Commerce (Secretaría de Comercio), in conjunction with the Department of Patrimony and Industrial Development (Secretaría de Patrimonio y Fomento Industrial), supply and demand patterns will be reviewed periodically to determine exportable volumes of cement. Similarly, and when necessary, domestic supplies may be increased to provide adequate regional supply.

- Attempts will be made to program the procurement of cement by the Public Sector on an adequate and timely basis.

CHAPTER IV

Obligations of the Productive Sectors

To the qualifications established for granting the various types of assistance provided by the Federal Government are added the following obligations on the part of the Productive Sector in support of the assistance established by this Development Program:

I To accomplish, as a minimum, the following expansions and new plant construction:

Firm and location	Start-up date	Capacity Ton/year
Cementos Tolteca, S.A. .... (?, D.F.)	February 1980	115,000
Sociedad Cooperativa Manufacturera de Cemento Portland La Cruz Azul, S.C.L. .... (La Cruz Azul, Hgo.)	July 1980	217,000
Cementos Tolteca, S.A. .... (?, Hgo.)	July 1980	550,000
Cementos Tolteca, S.A. .... (?, Jal.)	August 1980	100,000
Cementos Anáhuac, S.A. .... (?, Edo. de México)	September 1980	350,000
Cementos Mexicanos, S.A. .... (? Valles, S.L.P.)	March 1981	725,000
Cementos Maya, S.A. .... (Léon, Gto.)	March 1981	100,000
Cementos Apasco, S.A. .... (Macuspana, Tab. I)	May 1981	900,000
Cementos Tolteca, S.A. .... (Tula, Hgo.)	May 1981	280,000
Cementos Veracruz, S.A. .... (Orizaba, Ver.)	June 1981	900,000
Cementos Anáhuac, S.A. .... (Barrientos, Edo. de México II)	June 1981	500,000
Cementos Anáhuac, S.A. .... (Tamuín, S.L.P.)	June 1981	600,000
Cemento Portland Nactional, S.A. ..... (Hermosillo, Son.)(N)	July 1981	900,000
Cementos Mexicanos, S.A. .... (Monterrey, N.L.)	August 1981	725,000
Cementos Chihuahua, S.A. .... (Chihuahua, Chih.)	March 1982	600,000

Cementos Mexicanos, S.A. .... (Torreón, Coah.)	March 1982	725,000
Sociedad Cooperativa Manufacturera de Cemento Portland La Cruz Azul, S.C.L. .... (Lagunas, Oax.)	June 1982	1,188,000
Cementos Portland Moctezuma, S.A. .... (Tepetzingo, Mor.)(N)	August 1982	800,000
Cementos Guadalajara, S.A. .... (Guadalajara, Jal.)	December 1982	900,000
Cementos Apasco, S.A. .... (Macuspana, Tab. II)	June 1983	900,000
Cementos Mexicanos, S.A. .... (Not specified)(N)	June 1983	725,000
Cementos Anáhuac, S.A. .... (Not specified)(N)	June 1983	1,500,000
Cementos Tolteca, S.A. .... (Zapotiltic, Jal. II)	July 1983	900,000
Cementos Veracruz, S.A. .... (Not specified)(N)	February 1984	900,000

(N) = New plant

The development of the investment program will be monitored on a quarterly basis to evaluate fulfillment of the obligations established, pursuant to Article 22 of the Decree providing for Implementation of the National Industrial Development Plan.

(See this Decree, page 19-III-79 of the Industrial Decentralization Section)

II Payments for technical assistance shall not exceed 1.5% of the value of production.

III To make exports without affecting the national supply of the product. In general terms, it is hoped that the cement industry will make exports to compensate for at least 80% of the foreign exchange spent on machinery and equipment imports. Assuming that these imports represent 40% of the fixed assets and taking into account the surpluses that can be earmarked for export, the balance of foreign exchange for the 1980-1983 period, in millions of pesos, would be:

Year	Equipment Imports	Export of cement	Balance
1980	1,332	1,075	(257)
1981	5,629	1,504	(4,125)
1982	4,212	2,965	(1,247)
1983	4,024	6,866	2,842

The estimated figures in the preceding table show a balance of foreign exchange for the period in question, where cement exports compensate for 81.6% of equipment imports at 1980 prices.

IV In-plant delivery at the following prices:

Region and plant	F.O.B. Plant price for Bulk Gray Type I, Type II and Pozzolan Cement
NORTHERN BAJA CALIFORNIA	
Ensenada	$ 1.550.00
PACIFIC NORTH	
Hermosillo	$ 1.260 00
El Fuerte	$ 1.260 00
Mármol	$ 1.260.00
Guadalajara	$ 1.260.00
Zapotiltic	$ 1.260.00
NORTH	
Cd. Juárez	$ 1.270.00
Chihuahua	$ 1.270.00
Torreón	$ 1.270 00
Monterrey	$ 1.270 00
Del Norte	$ 1.270 00
Hidalgo	$ 1.270 00
Cd. Valles	$ 1.270 00
Tamuín	$ 1.270 00
León	$ 1.270 00
CENTRAL	
Mixcoac	$ 1.280 00
Atotonilco	$ 1.280 00
Tula	$ 1.280 00
Jasso	$ 1.280 00
Barrientos	$ 1.280 00
Apasco	$ 1.280 00
Jiutepec	$ 1.280 00
Puebla	$ 1.280 00
Acapulco	$ 1.280 00
SOUTHERN GULF	
Orizaba	$ 1.310.00
Lagunas	$ 1.310 00
Mérida	$ 1.310.00

Delivery to the work site at maximum prices to the public for purchases of 5 tons or more, and for smaller purchases, delivery to the distributor's warehouse, in the following locations, at the maximum price indicated:

Zone & location	Maximum price to the public delivered to work site for Bulk Gray Type I, Type II and Pozzolan Cement
NORTHERN BAJA CALIFORNIA	
Ensenada, B.C.N.	$ 1,870.00
Guerrero Negro, B.C.N.	$ 2,200.00
Tecate, B.C.N.	$ 2,030.00
Mexicali, B.C.N.	$ 2,080.00
Tijuana, B.C.N.	$ 2,030.00
S.L. Río Colorado, Son.	$ 2,100.00
PACIFIC NORTH	
Hermosillo, Son.	$ 1,550.00
Empalme, Son.	$ 1,730.00
Guaymas, Son.	$ 1,720.00
Caborca, Son.	$ 1,770.00
Nogales, Son.	$ 1,770.00
Cananea, Son.	$ 1,770.00
Cd. Obregón, Son.	$ 1,770.00
Santa Ana, Son.	$ 1,730.00
Agua Prieta, Son.	$ 1,810.00
Los Mochis, Sin.	$ 1,700.00
Huatabampo, Sin.	$ 1,720.00
Guasabe, Sin.	$ 1,720.00
Guamúchil, Sin.	$ 1,740.00
Santa Rosalía, B.C.S.	$ 1,950.00
Navojoa, Son.	$ 1,750.00
Escuinapa, Sin.	$ 1,720.00
Mazatlán, Sin.	$ 1,690.00
La Paz, B.C.S.	$ 1,920.00
Culiacán, Sin.	$ 1,740.00
San Lucas, B.C.S.	$ 2,110.00
Guadalajara, Jal.	$ 1,550.00
Ameca, Jal.	$ 1,700.00
Tepic, Nay.	$ 1,720.00
Atotonilco, Jal.	$ 1,710.00
Puerto Vallarta, Jal.	$ 1,760.00
La Barca, Jal.	$ 1,720.00
Ocotlán, Jal.	$ 1,710.00
Tala, Jal.	$ 1,690.00
Tuxpan, Nay.	$ 1,750.00
Santiago Ixcuintla, Nay.	$ 1,780.00
Tepatitlán, Jal.	$ 1,700.00
Autlán, Jal.	$ 1,740.00
Zacatecas, Zac.	$ 1,790.00
Tlaquepaque, Jal.	$ 1,680.00
Aguascalientes, Ags.	$ 1,730.00
Cd. Guzmán, Jal.	$ 1,680.00
Jiquilpan, Mich.	$ 1,720.00
Manzanillo, Col.	$ 1,730.00
Los Reyes, Mich.	$ 1,740.00
Zamora, Mich.	$ 1,740.00
Zacapu, Mich.	$ 1,750.00
Sahuayo, Mich.	$ 1,720.00
Apatzingán, Mich.	$ 1,810.00
Nueva Italia, Mich.	$ 1,790.00
Lázaro Cárdenas, Mich.	$ 1,870.00
Colima, Col.	$ 1,700.00
Uruapan, Mich.	$ 1,770.00
Tecomán, Col.	$ 1,720.00
NORTH	
Ciudad Juárez, Chih.	$ 1,560.00
Nvo. Casas Grandes, Chih.	$ 1,790.00
Villa Ahumada, Chih.	$ 1,730.00
Janos, Chih.	$ 1,750.00
Chihuahua, Chih.	$ 1,560.00
Santa Bárbara, Chih.	$ 1,790.00
Ojinaga, Chih.	$ 1,770.00
Aldama, Chih.	$ 1,700.00
Cuauhtémoc, Chih.	$ 1,720.00
Delicias, Chih.	$ 1,710.00
Ciudad Camargo, Chih.	$ 1,740.00
Jiménez, Chih.	$ 1,770.00

Zone & location	Maximum price to the public delivered to work site for Bulk Gray Type 1, Type II and Pozzolan Cement
Parral, Chih.	$ 1,790.00
Torreón, Coah.	$ 1,560 00
Matamoros, Coah.	$ 1,690 00
San Pedro de las Colonias, Coah.	$ 1,710 00
Parras, Coah.	$ 1,750 00
Cuencamé, Dgo.	$ 1,720 00
Guadalupe Victoria, Dgo.	$ 1,760.00
Durango, Dgo.	$ 1,780.00
Río Grande, Zac.	$ 1,780.00
Fresnillo, Zac.	$ 1,810.00
Santiago Papasquiaro, Dgo.	$ 1,850 00
Goméz Palacio, Dgo.	$ 1,560 00
Lerdo, Dgo.	$ 1,560 00
Monterrey, N.L.	$ 1,560 00
Linares N.L.	$ 1,730 00
Saltillo, Coah.	$ 1,720 00
Montemorelos, N.L.	$ 1,720.00
Monclova, Coah.	$ 1,760 00
Sabinas Hidalgo, N.L.	$ 1,710.00
Reynosa, Tamps.	$ 1,770 00
Villa Frontera, Coah.	$ 1,750.00
Nuevo Laredo, Tamps.	$ 1,770 00
Múzquiz, Coah.	$ 1,810 00
Nueva Rosita, Coah.	$ 1,790.00
Sabinas, Coah.	$ 1,790.00
Río Bravo, Tamps.	$ 1,770.00
Matamoros, Tamps.	$ 1,800.00
Valle Hermoso, Tamps.	$ 1,800.00
Matehuala, S.L.P.	$ 1,810.00
Guadalupe, S.L.P.	$ 1,730 00
Piedras Negras, Coah.	$ 1,850 00
Ciudad Acuña, Coah.	$ 1,870 00
Ciudad Valles, S.L.P.	$ 1,560 00
Río Verde, S.L.P.	$ 1,740 00
Ciudad Mante, S.L.P.	$ 1,720 00
Ciudad Victoria, Tamps.	$ 1,770 00
Temazunchale, S.L.P.	$ 1,720 00
Ebano, S.L.P.	$ 1,700 00
Tampico, Tamps.	$ 1,720 00
Papantla, Ver.	$ 1,810 00
Tuxpan, Ver.	$ 1,760 00
Poza Rica, Ver.	$ 1,770 00
Valle de Santiago, Gto.	$ 1,720 00
Ciudad Madero, Tamps.	$ 1,720 00
Coatzacoalcos, Ver.	$ 1,780 00
Loma Bonita, Ver.	$ 1,780 00
León, Gto.	$ 1,560.00
Allende, Gto.	$ 1,740 00
Arandas, Jal.	$ 1,740 00
San Luis Potosí, S.L.P.	$ 1,760 00
Cortazar, Gto.	$ 1,740 00
Guanajuato, Gto.	$ 1,710 00
Dolores Hidalgo, Gto.	$ 1,[illegible]20 00

Zone & location	Maximum price to the public delivered to work site for Bulk Gray Type I, Type II and Pozzolan Cement
Irapuato, Gto.	$ 1,710 00
Jacona, Mich.	$ 1,750 00
Salamanca, Gto.	$ 1,720.00
Jerez, Zac.	$ 1,800 00
Celaya, Gto.	$ 1,730 00
Lagos de Moreno, Jal.	$ 1,700 00
La Piedad, Mich.	$ 1,730 00
Salvatierra, Gto.	$ 1,750 00
San Juan de los Lagos, Jal.	$ 1,720.00
Sta. Cruz, de J. Rosas, Gto.	$ 1,720 00
Morelia, Mich.	$ 1,760 00
Moroleón, Gto.	$ 1,740 00
Pátzcuaro, Mich.	$ 1,760 00
San Francisco del Rincón, Gto.	$ 1,700 00
Silao, Gto.	$ 1,700.00
CENTRAL	
Tula, Hgo.	$ 1,570.00
Amecameca, Edo de México	$ 1,720.00
San Juan del Río, Qro.	$ 1,730.00
Pachuca, Hgo.	$ 1,720.00
Tulancingo, Hgo.	$ 1,730 00
Cd Hidalgo, Mich.	$ 1,770.00
Querétaro, Qro.	$ 1,750.00
Toluca, Edo. de Méx.	$ 1,720.00
Texcoco, Edo. de Méx.	$ 1,710 00
Zitácuaro, Mich.	$ 1,750.00
Distrito Federal	$ 1,700.00
Acámbaro, Gto.	$ 1,770.00
Cuernavaca, Mor.	$ 1,700 00
Ciudad Altamirano, Gto.	$ 1,790 00
Cuautla, Mor.	$ 1,710 00
Huetamo, Mich.	$ 1,810.00
Zacatepec, Mor.	$ 1,720.00
Taxco, Gro.	$ 1,740.00
Iguala, Gro.	$ 1,720.00
Puebla, Pue.	$ 1,570 00
Apizaco, Tlax.	$ 1,710.00
Mártinez de la Torre, Ver.	$ 1,790 00
Cholula, Pue	$ 1,700.00
Tlaxcala, Tlax.	$ 1,710.00
Huamantla, Tlax.	$ 1,720.00
Atlixco, Pue.	$ 1,710 00
Huachinango, Pue.	$ 1,760 00
Tehuacán, Pue.	$ 1,740.00
Sn. Martin Texmelucan, Pue.	$ 1,710.00
Tezutlán Pue.	$ 1,770 00
Huajuapan de León Oax.	$ 1,750 00
Acapulco, Gro.	$ 1,570 00
Tecpan, Gro.	$ 1,730 00
Chilpancingo, Gro.	$ 1,750 00
Zihuatanejo, Gro.	$ 1,780 00
Pinotepa Nacional, Oax.	$ 1,790 00

Zone & location	Maximum price to the public delivered to work site for Bulk Gray Type I, Type II and Pozzolan Cement	Zone & location	Maximum price to the public delivered to work site for Bulk Gray Type I, Type II and Pozzolan Cement
SOUTHERN GULF		Tehuantepec, Oax.	$ 1,760.00
Orizaba, Ver.	$ 1,600.00	Ciudad Cuauhtémoc, Chis.	$ 1,910.00
Córdova, Ver.	$ 1,730.00	Oaxaca, Oax.	$ 1,820.00
Veracruz, Ver.	$ 1,780.00	Comitán, Chis.	$ 1,870.00
Misantla, Ver.	$ 1,830.00	Tuxtla Gutiérrez, Chis.	$ 1,840.00
Jalapa, Ver.	$ 1,780.00	Huixtla, Chis.	$ 1,870.00
San Andrés Tuxtla, Ver.	$ 1,830.00	Tapachula, Chis.	$ 1,850.00
Santiago Tuxtla, Ver.	$ 1,830.00	Venustiano Carranza, Chis.	$ 1,880.00
Tierra Blanca, Ver.	$ 1,770.00	Sn. Cristóbal las Casas, Chis	$ 1,870.00
Alvarado, Ver.	$ 1,800.00	Villahermosa, Tab.	$ 1,940.00
Tuxtepec, Oax.	$ 1,790.00	Las Choapas, Ver.	$ 1,830.00
Coatepec, Ver.	$ 1,760.00	Mérida, Yuc.	$ 1,750.00
Acayucan, Ver.	$ 1,780.00	Progreso, Yuc.	$ 1,890.00
Juchitán, Oax.	$ 1,760.00	Campeche, Camp.	$ 1,940.00
Arriaga, Chis.	$ 1,800.00	Peto, Yuc.	$ 1,940.00
Ciudad Ixtepec, Oax.	$ 1,760.00	Chetumal, Q. Roo.	$ 1,980.00
Pijijiapan, Chis.	$ 1,840.00	Tisimín, Yuc.	$ 1,950.00
Tonalá, Chis.	$ 1,810.00	Valladolid, Yuc.	$ 1,930.00
Salina Cruz, Oax.	$ 1,780.00	Carrillo Puerto, Q. Roo.	$ 1,980.00
Minatitlán, Ver.	$ 1,790.00	Puerto Juárez, Q. Roo.	$ 1,990.00
Tenosique, Tab.	$ 1,910.00	Ciudad del Carmen, Camp.	$ 2,020.00

For localities not mentioned above, the maximum price to the public delivered to the work site shall be determined by adding to the price at the nearest locality the additional freight charges incurred.

When, for reasons of imbalance in regional supplies it is necessary to supply a plant different from the one located in a given zone, the Department of Commerce shall authorize the corresponding maximum price to the public delivered to the work site.

The price adjustments that may be required for sound operation of this industrial sector shall be determined on the basis of the variations registered in the cement production and distribution cost factors.

This Development Program for the Cement Industry shall enter into force on the day following its publication in the "Diario Oficial" of the Federation.

Done in Mexico City, Federal District, on June 30, 1980. -The Secretary of Finance and Public Credit, David Ibarra Muñoz.- Flourish. - The Secretary of Patrimony and Industrial Development, José Andrés Oteyza. - Flourish. - The Secretary of Commerce, Jorge de la Vega Domínquez. - Flourish.

Remittance No. 10 28-IV-81

RESOLUTION ON THE ADJUSTMENT OF CEMENT PRICES

(Published in the "Diario Oficial" of the Federation on April 28, 1981)

In the margin, a seal with the National Escutcheon, which reads: Estados Unidos Mexicanos.- Secretaría de Comercio (United States of Mexico.- Department of Commerce).

David Ibarra Muñoz, José Andrés Oteyza, Jorge de la Vega Domínguez, Secretary of Finance and Public Credit, Secretary of Patrimony and Industrial Development, and Secretary of Commerce, respectively, pursuant to Articles 31, Section IV; 33, Section XII; and 34, Section VII of the Organic Law of the Federal Public Administration; 1, 2, and other related articles of the Law on the Powers of the Federal Executive Branch in Economic Matters; 1, 2, 7, and other related articles of the Regulation of Articles 2, 3, 4, 8, 11, 13, 14 and 16-20 of said Law; 1, Section III, 3, 4, 5, 12 and other related articles of the Resolution establishing the procedures for setting the prices of the products indicated, published in the "Diario Oficial" of the Federation on October 25, 1977, as well as Chapter IV, Part IV of the Development Program for the Cement Industry, published in the "Diario Oficial" of the Federation on July 1, 1980, hereby issue the following:

RESOLUTION ON THE ADJUSTMENT OF CEMENT PRICES

For the purpose of fully complying with the penultimate paragraph of Chapter IV, Paragraph IV of the Development Program for the Cement Industry, published in the "Diario Oficial" of the Federation on July 1, 1980, the Department of Commerce shall, by official letter, notify producing companies of price adjustments necessitated by variations in the cost of producing and distributing Types I, II and pozzolan cement. Consequently, beginning on the date of effectiveness of the official prices announced to such firms by official letter, the prices published in the "Diario Oficial" of the Federation on July 1, 1980 shall be understood to be adjusted.

(See the Development Program cited, page 1-VII-80 of this Section)

This Resolution shall enter into force on the day following its publication in the "Diario Oficial" of the Federation.

Mexico City, Federal District, April 23, 1981.- The Secretary of Finance and Public Credit, David Ibarra Muñoz. - Flourish. - In the absence of the Secretary, this document is signed by the Under-Secretary of Industrial Development, Natan Warman. - Flourish. - The Secretary of Commerce, Jorge de la Vega Domínguez. - Flourish.

UNITED CEMENT, LIME, GYPSUM AND ALLIED WORKERS INTERNATIONAL UNION,
Elk Grove Village, Ill., October 17, 1983.

Congressman SAM GIBBONS,
Rayburn House Office Building,
Washington, D.C.

DEAR CONGRESSMAN GIBBONS: I am writing on behalf of 20,000 workers in the United States cement industry represented by our union, the United Cement, Lime, Gypsum and Allied Workers International Union. I write to you with a dual purpose of appraising you of the history of the industry and to address the threat and harm that Mexican cement imports are causing our members in the United States cement industry as a whole.

The U.S. cement industry has a history of striving for greater productivity through modernization and supportive and cooperative labor/industrial relations. In the last 30 years the industry has a strong track record in advancing its levels of productivity. In 1952 there were approximately 40,000 workers in the production of cement with an output of 0.64 tons per manhour. Today there are approximately 22,500 production workers with an output of 1.33 tons per manhour. These dramatic increases in cement productivity have been the result of a strong commitment by the industry to modernize and embrace the latest developments in technology. The increased productivity has also been the result of a cooperative working relationship between the union and industry, with a commitment to the shared goal of increasing productivity.

These efforts and accomplishments of the United States cement industry are being seriously threatened by cement imports from Mexico. Since the beginning of the year, cement imports from Mexico have increased approximately 150 percent and cement clinker imports have increased over 450 percent. It is our belief that these dramatic increases in cement imports have been the direct result of energy subsidies provided to the Mexican cement industry by PEMEX, the Mexican Government's wholly owned oil and gas monopoly. PEMEX provides heavy fuel oil to the Mexican cement industry at less than 1/20th of the world market price. The production cement is an energy intensive process and approximately 50 percent of the cost of a ton of cement is attributed to the cost of energy.

This subsidy cuts Mexican cement producers manufacturing costs virtually in half and creates a competitive advantage that no U.S. producer, no matter how efficient, can overcome.

Mexican imports are having an immediate and direct adverse impact on over 4,300 workers working in cement plants located throughout Texas, the Southwest and the Southeast. It is a strong belief or our union that the Mexican Government is definitely providing a subsidy to the Mexican cement industry and that should be recognized and addressed as such under our trade laws. We strongly urge you and your colleagues to address this issue by developing a measure that will reflect the true value of this subsidy such as a measure based on the export or world market price of this heavy fuel oil.

Sincerely,

THOMAS F. MIECHUR,
President.

Mr. HANCE. Thank you, Mr. Chairman.

Chairman GIBBONS. We appreciate your fine contribution to this committee. We hate to lose you to the Senate.

Would you come on over any time?

Mr. HANCE. Sure.

Chairman GIBBONS. Mr. Jones.

Mr. JONES. Thank you, Mr. Chairman.

I, too, want to welcome a friend and constituent who is on the panel today, Mr. Bill Calvert, who is chairman and chief executive officer of Agrico Chemical, which is in Tulsa, Okla. I also want to apologize for the fact that I have not been able to be here and will not be able to be here for the full hearing.

We have had some longstanding hearings scheduled in the Budget Committee that I am chairing on defense procurement. Those hearings are under way now and I have to get back to them.

I would like to submit a couple of questions for the record to Mr. Calvert to give some further attention and detail on the subsidy question, including how he would measure it.

Also I would like for him to get into the record what the impact of this is on, say, employment in our area of Oklahoma.

So I will have my staff submit these questions and Mr. Calvert can answer them for the record. I did want to welcome him to the committee and I think we will learn greatly from him as I have over the years.

I also see another old and dear friend behind the witness table, Judy Hope, who is obviously representing somebody here but I would like to welcome her to the committee, too.

Chairman GIBBONS. Fine, thank you, gentlemen.

Those will be a part of the record.

[The questions and answers follow:]

ANSWERS TO QUESTIONS TO THE AD HOC COMMITTEE OF DOMESTIC NITROGEN PRODUCERS, SUBMITTED IN WRITING BY REPRESENTATIVE JAMES R. JONES OF OKLAHOMA

Question 1. Mr. Calvert, what is your estimate of the amount of the subsidy on Mexican ammonia imports based on conditions as you see them today using your proposed remedy?

Answer. The amount of the subsidy today would be approximately \$35–\$40/ton. This compares to a market price today in the order of \$140–\$150/ton. At this market price level the industry is just barely covering cash costs, but losing money on a full-cost basis. Our gas costs alone for making ammonia are in the order of \$125–\$130 per ton. If our prices were not depressed by the amount of the subsidy, our industry could return to financial health and re-start our plants in the U.S. The basis for this estimate of the subsidy is set out in detail in our written statement.

Question 2. Mr. Calvert, suppose that Mexico changed its natural gas policy and permitted U.S. companies to buy Mexican gas at the wellhead for export purposes. How would you, as a businessman, decide how much the Mexican gas was worth? What role would historic contract prices play in your decision?

Answer. The starting point for valuation of the Mexican gas would be prices in the competitive free market in the United States. I would first find the best offer currently available from U.S. suppliers for comparable quality gas in comparable volumes delivered to my U.S. plant. I would next determine the cost of transporting the Mexican gas from wellhead to my plant. The delivered price of U.S. gas less the transportation cost for the Mexican gas would establish the free market value of the Mexican gas at the wellhead.

Currently, gas can be purchased in the marketplace for about \$3.00 and up for deliveries in the range of 40,000 MMBTU's per day, depending on plant location. Assume that Mexican gas would compete at the lowest range of \$3.00–\$3.25 m.c.f. at the U.S. border, which is probably about right. Our best information is that the Mexican cost to transport gas to the U.S. border is approximately 95¢/m.c.f. I would thus buy Mexican gas the wellhead for any amount less than $2.05–$2.30/m.c.f.. That is at least $1.50/m.c.f. more than the current Mexican domestic price to industrial users.

Historic contract prices would play no role in finding the current value of Mexican gas. In a free market, Mexican gas would compete with current offers of U.S. gas, not gas sold under contracts made fifteen or twenty years and no longer available in the market.

Mr. Donald V. Borst of CF Industries has additional information on this latter issue and a historic perspective on what has happened to the U.S. ammonia industry in the last few years that has brought the industry to this point.

SUPPLEMENTAL ANSWER OF DONALD V. BORST

U.S. ammonia producers with low cost natural gas contracts are clearly not the cause of the industry's present low prices as some have alleged. This is clearly shown by CF Industries' own experience. CF has four world scale ammonia plants at Donaldsonville, Louisiana. Two are operating on a direct sale gas contract during the 1960's These two plants are operating. The other two plants built during the mid-1970's are faced with gas supplies at current market prices. These two plants are not operating because CF would incur losses at market prices set by low priced imports.

Last fall, CF has to make the painful decision to permanently close three ammonia plants located in North Carolina, Tennessee and Nebraska. These plants, along with their facilities to upgrade ammonia into the nitrogen fertilizers used by the farmers in those areas, were shut down and written off at a cost of $40 million. The plants could not be expected to compete with the cost-price squeeze between high cost interstate gas and low nitrogen fertilizer market prices. In fact, two of these plants has been receiving part of their gas supplies based on Mexican gas imported by the pipelines at $4.40 to $4.94/MMBTU.

It's ludicrous to say that because we have two plants operating on low priced gas that we would drive ammonia prices down to a level which caused us to idle two world scale plants and write off $40 million in closing three plants. Analysis readily shows that imported ammonia from Mexico is priced at the cash cost of domestic producers with market level gas contracts.

Since 1978, subsidized nitrogen imports have been rising regardless of market demand. During the last two years, U.S. agricultural nitrogen consumption declined by 23 percent due to a bad agricultural economy and the PIK program.

During the same period, U.S. ammonia production fell by 29 percent and domestic inventories climbed by 10 percent. But imports increased by 9–10 percent.

How can imports increase by this amount in the face of falling demand? The answer is simple: Subsidized, low-priced imports. Prices have been driven down below most U.S. producers' production costs and, in many cases, below the U.S. producer's cost of natural gas alone.

This has resulted in significant levels of permanent ammonia plant closures, as well as the idling of a major portion of the remaining U.S. ammonia capacity.

Prior to the beginning of the import problem in late 1978, the U.S. industry closed 20 plants (2.6 million tons/year ammonia capacity) as a result of overexpansion in the mid-1970's. Since 1978 and the onslaught of nitrogen imports, another 20 plants (3.3 million tons/year ammonia capacity) have been closed.

Furthermore, at the present time 19 percent (3.6 million tons/year ammonia capacity) of the remaining U.S. ammonia capacity has been idled and many operating plants are not running at full rate.

If this trend continues, more and more U.S. ammonia capacity will close as subsidized imports continue to penetrate the U.S. nitrogen market. It's just a matter of how fast additional capacity is installed in gas rich countries based on subsidized natural gas prices, and how much of the additional nitrogen production is forced into the U.S. market. If Congress does not act against two-tier raw material pricing, a major signal will be sent to the gas rich countries and the U.S nitrogen market will be be up for grabs.

Question. 3. Mr. Calvert, please give me an idea of what the impact of Mexican two-tier pricing of natural gas is on employment in Northeastern Oklahoma. I hope you can include in your response the indirect impact (e.g., natural gas price increases on other consumers of natural gas) as well as the direct effect on petrochemical companies such as your own.

Answer. The Oklahoma nitrogen fertilizer manufacturing industry currently is the second largest in the nation, accounting for in excess of 13 percent of the nation's production. It supplies product to farmer in all 77 of Oklahoma's counties.

28-466 O—83——6

The most recent data available shows a total operating budget of $300 million, with $288 million of that paid directly to Oklahoma workers and suppliers. In 1982, it was estimated that the industry generated $17 billion in State taxes and approximately $1.8 million in revenues to local taxing authorities.

If the Oklahoma nitrogen manufacturers have to shut down because they cannot compete with subsidized imports of ammonia, then not only will about 800 people in Oklahoma lose their jobs, but, in addition, it will obviously have a huge adverse impact on the State's economy and on tax revenues.

With reference to the indirect impact, the Oklahoma nitrogen industry accounts for about 30 percent of Oklahoma Natural Gas Company (ONG) sales, generating in excess of 40 percent of ONG's annual net operating income. Based on an analysis of a recent rate order for the Oklahoma Corporation Commission, it was estimated that the fertilizer producers are directly subsidizing other customers by $17.2 million annually. This analysis also indicated that ONG's other customers would be required to bear an additional $32 million annual in fixed costs if the fertilizer producers shut down.

Question 4. Mr. Jaquier, is there a possibility that nonmarket economies and other countries which might be affected by trade remedy laws would retaliate by curtailing grain purchases from the U.S.?

Answer. I cannot say whether some countries might retaliate for political reasons, even if our laws only offset their subsidies on these exports. There is little likelihood that any such retaliation would have any significant effect on total U.S. grain exports, however. The U.S. is the residual supplier of grain to the world. During the past four years, U.S. coarse grain inventories have fluctuated year-to-year by as much as 36.5 million metric tons or 105 percent. The inventory position of major competing countries in total has varied by no more than 2.4 million metric tons. Foreign production can be expected to be marketed regardless of the U.S. export position through the subsidy actions of central governments. The maximum U.S. vulnerability to cutoff of coarse grain exports due to trade reprisals by any specific country can be estimated to be no more than 2–2.5 million metric tons, the typical year-to-year swing in coarse grain inventories held by competing nations. This equates to about 3–5 percent of U.S. coarse grain trade. Any greater shift of business from the U.S. could be expected to open up substitute markets for U.S. grain. Those countries still buy grain, and total demand does not drop. Some countries simply shift to other suppliers. Over a period of several years, the U.S. vulnerability could be expected to approach zero as foreign inventories were depleted.

A detailed analysis of this point is included in the Ad Hoc Committee's written tesitmony.

In addition, the opponents of this amendment have argued that this will raise fertilizer prices to U.S. farmers. Our answer is that prices must rise enough to cover production costs of most U.S. producers and those exporting producers whose governments are not subsidizing their production costs, if U.S. farmers are to have adequate supplies of fertilizer when they need it. The U.S. nitrogen industry cannot continue to exist at the price levels which have been induced by subsidized foreign imports, but a price increase to the U.S. farmer has been grossly exaggerated. Today U.S. farmers are paying 18–30¢/bushel of corn (8–13 percent of production cost ex land) for nitrogen fertilizer. An incremental increase in price of 10 percent would only increase farmers' costs 2–3¢/bushel.

A healthy and competitive U.S. industry will continue to supply vital fertilizer, good years and bad, to meet the farmers' seasonal requirements. The American farmer will be assured of the most efficient distribution and storage system in the world, which is financed virtually at cost by domestic nitrogen producers. This distribution system stores production from plants which must be operated year-round, transports fertilizer from production point to the field, and has the capability of delivering to the U.S. farmer an entire year's requirement in a time span of 5–6 weeks. If U.S. producers start shutting down their plants, you cannot sssume that these foreign governments will maintain that system at its current efficient and low cost level, if at all. Maintenance of a competitive and efficient U.S. industry is necessary if the American farmer is to be assured of a future supply which will be insulated from the vagaries of world politics.

The American farmer is thus also insulated from possible cartel pricing of foreign nitrogen producers, which could result should the U.S. nitrogen industry be forced out of business by subsidized imports. In that event, the price of fertilizer would rise to much higher levels than would be the case if the U.S. industry stays healthy and remains in business.

Question 5. Mr. Jaquier, if we amend our countervailing duty law to provide that the two-tier pricing of natural resources constitutes a countervailable subsidy, aren't we opening our companies up to foreign retaliation, since the U.S. has as many or more subsidies than many other countries?

Answer. There are really two parts to your question. The first is the likelihood or not of possible retaliation by other countries refusing to buy some of our products or retaliation by imposing other trade barriers to U.S. goods, particularly U.S. petrochemical exports. The second part of the question is whether the U.S. subsidizes some of our production inputs, such as natural gas.

Some opponents to amendments to U.S. law to countervailing against subsidized natural resource product inputs, regardless of our legal right to do so, have raised the specter of retaliation. We have already addressed the likelihood of ineffective retaliation on U.S. grain exports in the previous question. We also recognize that this issue arose during the textile negotiations with China, during which period China cut back on grain purchases. It appears that that situation is distinguishable from possible retaliation by the Soviet Union or Mexico on U.S. grain and other agricultural exports. That trade with China was a new market that has just opened to U.S. trade.

The other allegation relates to possible retaliation against U.S. petrochemical exports, particularly by our major trading partners in Europe, on the basis that the U.S. regulation of natural gas prices in this country constitutes a similar subsidy to that addressed by the proposed legislation. Without arguing whether that might have been the case in the past, it is clearly an invalid argument today. The vast majority of U.S. petrochemical producers, and particularly U.S. nitrogen fertilizer producers, currently pay market clearing prices or above for their natural gas feedstocks. U.S. fertilizer producers are exporting at prices which fully account for those costs where those exports are competitive with prices established by Soviet and Mideast producers in the European market and other world markets. To the extent competitive world prices are inadequate to cover such U.S. producer costs, U.S. producers cannot compete long term with such prices by selling at a loss.

The principal problem in world nitrogen fertilizer markets over the past year has been in prices of urea. Urea supplies have been a glut on world markets as a result of overproduction by many countries relative to world demand. It appears likely that urea has been selling at dumped prices recently, even in the U.S. market, as a result. While dumping cases on urea have been considered by some U.S. producers, the same problem exists with regard to subsidized natural gas inputs to produce ammonia, which is in turn passed through as an upstream subsidy in the production of urea, with regard to certain countries. If U.S. trade laws are inadequate to address the upstream subsidies problem on ammonia, they may be inadequate to effectively address dumping of urea, since the current practice by the Commerce Department is to calculate production costs based on the subsidized cost of the natural gas input.

In the future, to the extent U.S. petrochemical producers are required to compete in world markets with lower priced petrochemicals produced by countries with a real comparative advantage in natural gas, U.S. petrochemical exporters may lose business in world markets to such producers. However, U.S. petrochemical producers will also be forced to compete with subsidized petrochemical products from some countries if natural gas subsidies are allowed to continue to distort trade in world markets. Such subsidy practices also distort prices for producers in other countries which are trying to compete fairly, based on comparative advantage.

The Congress may be unable to effectively address such subsidies by other countries in world markets under U.S. trade laws, but the Congress must address such subsidized products entering U.S. markets in order to effectively argue that other governments should also offset such subsidies in their markets, thereby removing this unfair trade distortion. Otherwise, there are only two alternatives. U.S. producers will be forced to withdraw from world export markets and shut down U.S. production by that amount, or the U.S. Government would have to subsidize such exports in order for U.S. producers to maintain their market share in those world markets. It is unlikely and even unthinkable that the U.S. should embark on such a subsidy program, and the U.S. industry has not requested such action.

This problem is not dissimilar to that being currently faced by U.S. agricultural exporters and U.S. farmers who are being forced to compete with subsidized products, such as wheat flour and pasta, as well as direct subsidies of grain exports. The free market trading system in world markets simply cannot survive such a subsidy trade war, and most governments simply cannot afford or justify such subsidies, including the U.S. Government. These subsidy problems in world markets are a direct result of the increasing direct intervention by governments in the marketplace, and we believe that the U.S. Government should take the lead by effectively offsetting such subsidies in its markets and urging other governments to do the same through GATT or through direct negotiations with non-GATT members.

Virtually all governments engage in some "subsidies" domestically through tax policies, general economic policies and public support of basic infrastructure. Such subsidies are acceptable and recognized in the world trading system, but they are to be limited to such domestic policies. The GATT Articles and the Subsidies Code require that GATT members and Code signatories not direct or pass through such subsidies in their exports. Even developing countries are obligated to avoid trade distortions and injury to other producers by reason of their development policies. The United States has fewer of such subsidies than virtually all other countries who participate in world trade. Where such subsidies have been deemed to exist, such as in DISC, the U.S. Government has undertaken to eliminate them.

Mr. CALVERT. Thank you very much.

Chairman GIBBONS. Next Mr. Thomas E. Bronson, president of the Moore-McCormack Cement Co.

STATEMENT OF THOMAS E. BRONSON, PRESIDENT, MOORE-McCORMACK CEMENT CO., INC., ON BEHALF OF COALITION OF U.S. CEMENT PRODUCERS AND WORKERS

Mr. BRONSON. Thank you very much, Mr. Chairman. I appreciate the opportunity to testify about the urgent need for legislation to provide some remedy for one of the most devastating subsidies being provided by foreign governments to their domestic industries.

This hearing as we understand it is about subsidies that occur when a foreign government dictates that some natural resource and energy source or feedstock must be provided to domestic industries at a price below the fair market value of that natural resource.

In the case of Mexico the subsidies provided Mexican cement producers are for the stated and expressed highly visible purpose of enhancing exports from that country.

We market cement in 17 States in the eastern half of the United States. As president of Moore-McCormack Cement Co. we are experiencing at this time firsthand the harmful and potentially catastrophic effects of the kind of subsidy that gives rise to this hearing. The Government of Mexico provides heavy fuel oil, electricity and other energy sources to Mexican cement companies at an enormously preferential price. This undisputably by reason of Government action gives Mexican cement companies an unfair and completely artificial advantage in the marketplace for the production and sale of cement.

Mr. Chairman, I want to make it very clear that none of us, I believe, on this panel and certainly none of us in the cement industry are here today to ask for any protection against legitimate foreign competition. We don't need help on that score. We commenced investing in cement in 1973. We knew what the future outlook for oil prices, energy prices was likely to be. We knew that we had to be competitive in the future with foreign competition.

We never realized we might have to be competitive with our own Government. Our plants are among the most efficient in the world and our labor the same. Our technology is at the leading edge of this field not only in the United States but throughout the world. Our company and the vast majority of cement producers are capable of competing with any Mexican producers on a head-to-head basis. We don't need protection, Mr. Chairman, but we need a remedy against foreign companies that can obtain fuel from their government at a tiny fraction of the marketplace, particularly in those cases where the foreign government does it for the purpose of correcting its own economic woes.

In this particular case their economic woes are being exported to the United States and the people on this panel are receiving a disproportionate burden of this policy. No cement company, however efficient, however effective, can compete against another that benefits from the enormously preferential energy prices available to Mexican Government's companies by Government decree.

In fact our efficiency, I would like to point out, is even sufficient to allow us to absorb the higher cost of capital in this country than in our trading competitors' foreign countries, the unfavorably taxing policies of this country when compared to foreign countries, and the ability to absorb the financial burden of the more stringent environmental regulations this country's governmental policy imposes on its industries as opposed to foreign countries.

We believe the Mexican fuel subsidies are contrary to the letter and the spirit of current U.S. law and the GATT. Yet the ITA, the agency responsible for enforcing our import laws, has adopted a policy of interpreting our laws as if they don't apply to those subsidies.

In fact the ITA has embarked it would appear on a policy that would appear to be designed to wipe out the U.S. cement industry if it were allowed to stay in place.

I am here to testify in support of the subcommittee's proposal to require the imposition of a countervailing duty against imports that benefit from foreign government subsidies on fuels and other natural resources.

First, let me emphasize the sheer magnitude of the Mexican energy subsidies. The Government of Mexico is providing Mexican cement companies with fuel oil at approximately one-twentieth of the free market price. Obviously the benefit to Mexican cement producers is enormous.

We have estimated that a moderate efficient cement plant in Mexico would incur costs of $14.96 per ton if it purchased fuel at $27.30 which is the Pemex government-owned monopoly export price. In fact such a plant would incur costs at only 68 cents per ton at the Mexican Government-subsidized price of $1.23 per barrel.

The resulting savings of $14.28 per ton amounts to between one-fourth and one-third of the average cement price in the United States.

Mr. Chairman, our experience in Florida signals a grim message for American industry. This subsidy coupled with an ITA's interpretation obviously has the potential to render our cement investments worthless. What is the magnitude of these imports? Two years ago in 1981 there was no Mexican cement imported into Florida according to the Department of Commerce. In all of 1982 only 12,558 tons of cement were imported in Florida.

In August 1983, the most recent month for which Commerce Department figures are available, 32,482 tons of Mexican cement came into Florida alone. That is 2.5 times as much cement imported in 1 month as during all of 1982.

If 1983 imports continue at the present level, over one-quarter million tons of Mexican cement will be imported through Tampa and Miami alone, more than 20 times as much in 1982.

I think it is very clear what the intentions are of the Mexican cement producers with respect to the export of cement into the United States.

Earlier this year when they first bought a terminal in West Palm Beach for some $7 million or $8 million to facilitate the import of cement, they made it clear in the marketplace that they were prepared to sell cement at whatever price, and they certainly by reason of this testimony we can see they can afford to sell cement at whatever price it takes to move whatever volumes they care to move to capture the market share in the United States.

I might also say that here in the last month or two I think not coincidentally after these proceedings started, of course, they have become much quieter with respect to the marketplace. That doesn't mean the competitive advantages these subsidies provided do anything but allow them to continue to expand shipments to the United States.

We are not talking about a southwest Florida problem or Southwest U.S. problem, nor a Florida problem. With their subsidy advantages Mexican companies can push their subsidized cement into any of our coastal States up the Ohio River and Mississippi River and even into the Great Lakes.

Based on our experience in Florida, and we have experienced a 2,000-percent increase in 1 year, I believe the Mexicans will go after some or all of those markets unless this country and this Congress insures that American industry should not be the victim of this type of subsidy program.

Moore-McCormack Cement would support any test that fairly compensates for the difference between the controlled domestic price and the fair value of the fuel oil or other resource. The first alternative under consideration today for measuring the amount of subsidy is the difference between the controlled domestic price and the export price and would provide an excellent measure of the true value of subsidies like the Mexican fuel oil subsidy.

There may be other measures such as a fair price on world markets that would provide an equally fair and predictable benchmark. Indeed there is something to be said for specifying alternative measures of the fair value price.

In summary, Mr. Chairman, we believe that the proposed legislation addresses a problem of great importance to many American industries. I find it difficult to find any reason that any Congressman of the United States would not be heavily influenced and persuaded by the grim outlook that this kind of ITA interpretations can have on American industry.

To be effective we believe that the legislation should rely on a simple and accurate measure of the fair value of the resource being subsidized such as export price or world market price.

Only if such a standard is in place and enforced will American companies be able to compete on a fair and equal basis with foreign companies whose natural resource costs are almost completely eliminated by government action.

Mr. Chairman, I thank you very much for the opportunity to appear before your committee.

[The prepared statement follows:]

STATEMENT OF THOMAS E. BRONSON, PRESIDENT, MOORE-MCCORMACK CEMENT CO., INC.

Thank you, Mr. Chairman. I very much appreciate the opportunity to testify this morning about the urgent need for legislation to provide some remedy for one of the most devastating subsidies being provided by foreign governments to their domestic industries. These subsidies occur when a government dictates that some natural resource--an energy source or a feedstock--must be provided to domestic industries at a price below the fair market value of that natural resource. As President of Moore-McCormack Cement Company, I have experienced at first hand the harmful effects of one subsidy of this type. The Government of Mexico provides heavy fuel oil, electricity and other energy sources to Mexican cement companies at an enormously preferential price. The largest subsidy is the one on fuel oil, which is provided to Mexican domestic cement companies at about one-twentieth of the Mexican export price. This gives Mexican cement companies an unfair and completely artificial advantage in the marketplace.

These Mexican subsidies pose a very serious threat to free trade. As you know better than most people, Mr. Chairman, this country has worked for years, through participation in the GATT and through our domestic legislation, to create new opportunities for free and fair international trade. The United States and our trading partners renewed that commitment most recently in the Tokyo Round of multilateral trade negotiations, and you in Congress confirmed that commitment in the 1979 Trade

Agreements Act. One of the basic principles of those GATT negotiations and the 1979 Act was that no country should be able to create an unfair trade advantage by subsidizing its domestic industries. Mexico, as you know, has never signed those trade agreements. And now the Government of Mexico is giving energy-intensive industries like the cement industry a tremendously unfair advantage, by virtually giving away fuel oil and other energy sources.

Mr. Chairman, I am not here today to ask for any protection against legitimate foreign competition. Moore-McCormack does not need any help on that score. Our plants are among the most energy-efficient in the world, and our labor among the most productive. Our company and the vast majority of U.S. cement producers are capable of competing with any of the Mexican producers on a "head-to-head" basis. We don't need any protection, Mr. Chairman--but we do need a remedy against foreign companies that can obtain fuel from their government at a tiny fraction of the market price. No cement company, however efficient, however competitive, can compete against another that benefits from the enormously preferential energy prices available to Mexican companies by government decree.

Moore-McCormack Cement commenced investing in cement production capacity as early as 1974. This was a time when we and the rest of the world were seeing energy prices skyrocket. We designed a plant then, as it is now, as efficient in fuel economy as any in the world. Additionally, our electrical consumption in our Brooksville plant is among the most efficient for the type of manufacturing process used. Our raw materials cost and labor cost also favorably compare with the most efficient producers. We have invested, heavily relying on a conviction that we should not invest unless we could compete with the most efficient of foreign producers. While we recognized the necessity for effectively competing with foreign producers, it never occurred to us that our government, while espousing the necessity for increasing international trade, would turn its back and ignore unfair subsidies as is the case with the Mexicans. This fact has made it impossible for us to compete and thus could render our investment worthless if the Mexican penetration of our markets continues at the current rate due to Mexican government subsidization of cement production.

We believe that the Mexican fuel subsidies are contrary to the letter and the spirit of current U.S. law and of the GATT. Yet the ITA, the agency responsible for enforcing our import laws, has adopted a policy of interpreting our laws not to apply to those subsidies. Moore-McCormack participated actively in the recent countervailing duty case against cement from Mexico, in which the ITA reaffirmed its position from earlier cases, that Mexico's preferential energy pricing system is not a countervailable subsidy. Because we have not been able to obtain relief under the existing countervailing duty law, I am here today to testify in support of the Subcommittee's proposal to require the imposition of a countervailing duty against imports that benefit from foreign government subsidies on fuel and other natural resources. Specifically, we recommend that the Subcommittee introduce legislation that would measure the fair value of the natural resource in question. Fair value should be gauged by some clear, objective standard, such as the foreign country's export price. That approach would offer the most complete, most precise and fairest remedy for the amount of subsidy being provided.

First, I want to emphasize the sheer size of the Mexican energy subsidies. In February 1983 (as the countervailing duty petition noted), Mexican cement companies could purchase heavy fuel oil from PEMEX, the Government-owned oil company, for the equivalent of $1.23 per barrel. At the same time, the price at which PEMEX made the same type of oil available for export was $27.30 per barrel. That is a difference of over 2,000 percent. Moreover, the world market price for heavy fuel oil in February 1983 was between $25.00 and $30.00 per barrel, depending on point of delivery. In other words, the Government of Mexico is providing Mexican cement companies with fuel oil at approximately one-twentieth of the free market price.

The benefit to Mexican cement producers is enormous. The countervailing duty petition estimated--and this estimate was not disputed by the Mexicans--that the modern Mexican plant of Cementos Mexicanos, located in Ensenada, Baja California, which uses the more energy-efficient "dry" process, would incur fuel costs of $14.96 per ton if it purchased fuel at $27.30 per barrel, the PEMEX export price. In fact, the Ensenada plant incurred costs of only 68 cents per ton, at the subsidized price of $1.23 per barrel. The resulting savings of $14.28 per ton amounts to between one-fourth and one-third of the selling price of cement in U.S. markets.[1]

The impact on the U.S. market is not theoretical. Import statistics show that there was an increase of more than 500 percent in imports of Mexican cement into the United States between 1981 and 1982. 1983 import figures show that the trend is continuing.

Mr. Chairman, our experience in Florida carries a grim message for American industry. The tremendous advantage created by Mexico's fuel price subsidies enables Mexican industries to enter markets in which they could not ordinarily compete. For example, markets for cement normally are regional, since transportation over long distances is comparatively expensive. However, the cost advantage provided by the fuel subsidy enables Mexican cement companies to absorb higher transportation costs than would be acceptable to a cement company purchasing energy

---

[1] According to the July 1983 monthly cement industry report prepared by the Bureau of Mines, U.S. Department of the Interior, the average F.O.B. plant selling price of cement in the United States in 1982 was $51.43 per ton.

at market prices. Indeed, the Mexican company that produces most of the cement exported from Mexico to Florida is located near Tampico, which is hundreds of miles away from Florida. Until recently, no cement from that source was shipped into Florida. However, the cost advantage due to the fuel subsidy is so great that the Mexicans now can truck their cement to a port, load it onto a ship, send the ship to a terminal in Florida, unload the cement back onto trucks or rail cars, ship it to the customer, and still beat the best price of local U.S. cement producers.

Thus, the problem is not limited to states like Texas and California, which share a border with Mexico. The $14.28 per ton subsidy advantage that the Mexicans receive for fuel oil is enough to pay transportation costs 200 to 250 miles inland from any U.S. river or ocean port. Anywhere within that radius, the Mexican producers have the ability to undersell any comparably efficient American plant--not because of any legitimate competitive advantage, but solely because of Mexican Government fuel subsidies.

Two years ago, in 1981, there was no Mexican cement imported into Florida, according to the U.S. Department of Commerce. In all of 1982, only 12,558 tons of cement from Mexico were imported into Florida. In August 1983, the most recent month for which Commerce Department figures are available, 31,482 tons of Mexican cement came into Florida alone. That's two and one-half times as much cement imported in one month as during all of 1982. During the first eight months of 1983, 164,594 tons of Mexican cement came into Florida. That's over thirteen times as much as in all of 1982. If 1983 imports continue at their present level, over one-quarter of a million tons of Mexican cement will be imported through Tampa and Miami alone--more than twenty times as much as in 1982. In other words, Mr. Chairman, we are seeing a two thousand percent increase in cement imported from Mexico to Florida during a single year.[2]

Mr. Chairman, what I am saying is that this problem is not limited to the Southwest. It is not limited to Florida. With their artificial cost advantage, Mexican companies can push their subsidized cement into any of our coastal states, up the Mississippi River, and even into the Great Lakes. And based on our experience in Florida--a two thousand percent increase in one year--I believe that the Mexicans will go after some or all of those markets unless this country and this Congress decides that American industry should not be the victim of this type of subsidy program.

As you know, U.S. companies in the cement industry and in other impacted industries have actively pursued their remedies under existing countervailing duty laws. Countervailing duty

---

[2] Import statistics in this paragraph are taken from U.S. Dept. of Commerce, Bureau of the Census data on U.S. imports from Mexico of portland hydraulic cement (other than white nonstaining) by customs district (IM 145X).

petitions were filed by the cement industry,[3] the anhydrous ammonia industry,[4] and the carbon black industry.[5] Each of those petitions sought to impose a countervailing duty against Mexican fuel subsidies, as well as other Mexican subsidy programs. In each case, the ITA held that the fuel subsidies were "generally available" to all Mexican industries and so were not countervailable.

We believe that the ITA's interpretation of the existing countervailing duty law is unreasonable, inconsistent with the intention of Congress in enacting the Trade Agreements Act, and contrary to U.S. court decisions in countervailing duty cases. Our countervailing duty law,[6] and court decisions interpreting it,[7] provide that every form of foreign subsidy is countervailable unless it is provided to all industries. The Mexican subsidies are provided disproportionately to a small,

---

[3] 48 Fed. Reg. 14,019 (April 1, 1983).

[4] 47 Fed. Reg. 53,440 (Nov. 26, 1982).

[5] 47 Fed. Reg. 54,526 (Dec. 3, 1982).

[6] Sections 303 and 771(5) of the the Tariff Act of 1930, as amended, 19 U.S.C. §§ 1303, 1677.

[7] U.S. Steel Corp. v. United States, No. 82-101-1361, Slip Op. No. 83-53 (Ct. Int'l. Trade 1983) (rail subsidy countervailable unless provided to all products shipped under same conditions); Carlisle Tire and Rubber Co. v. United States, No. 79-5-748, Slip Op. No. 83-49 (Ct. Int'l Trade 1983) (countervailable subsidy is one not available to all manufacturers and producers); ASG Industries, Inc. v. United States, 467 F. Supp. 1200, 1213 (Cust. Ct. 1979) (any subsidy, including a government-mandated reduction in the cost of a factor of production, is countervailable).

specialized group of industries. Fuel oil at the preferential price may be purchased only by Mexican manufacturing companies that will consume the fuel themselves in Mexico. The preferential price is not available to Mexican companies wishing to use the fuel oil in operations outside Mexico. The preferential price is not available to Mexican companies wishing to resell the fuel oil or to export it. The group of industries eligible to purchase fuel oil at the preferential price excludes all foreign companies, all resellers, all exporters, and all Mexican companies that cannot consume the fuel oil themselves. What remains is a specialized group of industries that consume heavy fuel oil in their in-country manufacturing process.

The present situation must be distinguished from the case where the government would provide cheap fuel oil unconditionally to all purchasers. In that situation, none of the low-priced oil would be used to make cement in Mexico. The entire available supply would be purchased by brokers and resold for large profits on the world market, until the Mexican domestic price equaled the world price. Let me add that, if Mexico sold fuel oil to all comers at $1.23 per barrel, Moore-McCormack Cement would be first in line to buy it. By expressly forbidding exportation of low-priced oil and restricting sale of low-priced oil to resident end-users, the Government of Mexico is providing a direct subsidy specifically targeted at energy-intensive domestic industries, such as the cement industry.

The Mexican Government's preferential fuel prices are not just "domestic" subsidies aimed at improving the Mexican economy. They are specifically intended to increase exports. The subsidies are provided under the 1979 "National Industrial Development Plan." The official English language summary of that Plan states that a key policy of the Plan is "the principle of maintaining, at a lower level than the international one, the domestic price of industrially-used energy sources and basic petrochemicals," a policy whose goals include "the promotion of exports and the efficient substitution of imports." Moreover, the full Spanish language text of the Plan states that the preferential energy price program is intended as "a direct incentive for exports."

The value of preferential fuel prices as an export incentive clearly is higher for energy-intensive industries, such as cement. Energy costs account for as much as 50 percent of a cement company's total production costs. Obviously, preferential energy prices confer a much greater benefit, in both total dollar and percentage terms, on an industry like cement than on another industry where energy is, say, 10 percent of production costs. And that fact is not lost on the Government of Mexico, which, through its fuel price subsidies, has consciously targeted energy-intensive industries and consciously set out to use the fuel subsidy to increase exports in those specific industries.

28-466 O—83——7

We repeatedly presented the foregoing arguments to the ITA during the course of the Cement countervailing duty proceeding. Nevertheless, the ITA rigidly adhered to its now familiar position that such practices are not countervailable. I have come here today to express strong support for legislation that would correct what I believe to be the ITA's erroneous reading of the present law, and would provide some protection for U.S. companies against foreign attempts to use cheap natural resource supplies to capture U.S. markets for manufactured products. Let me stress once again that I am not seeking protection for some inefficient U.S. producer against an efficient foreign industry. Rather, I am looking for a remedy against foreign producers that are able to push large quantities of cement into the United States at predatory prices solely because the Mexican Government is providing them with huge energy subsidies.

Countervailing duties against the Mexican Government's preferential-priced fuel subsidies, and similar natural resource-based subsidies, can only be effective if they offset the full value of the subsidy to foreign manufacturers. Indeed, under the Trade Agreements Act of 1979 and the GATT Subsidies Code, we are required to determine precisely and objectively how much subsidy is being provided and impose a countervailing duty for that amount. In order to make that calculation, the ITA must determine a fair value with which to compare the subsidized price. The countervailing duty should equal the difference between the fair value and the subsidized price.

Moore-McCormack Cement would support any subsidy test that fairly and accurately compensates for the difference between the controlled domestic price and the fair value of the fuel oil or other resource. Ideally, the benchmark price would be the arm's-length, free market price. However, the legislation you are considering would by definition apply only when there was no domestic free market price in the country under investigation for the product in question. For example, the Mexican Government through PEMEX controls the domestic price of fuel oil; there is no domestic free market price. Thus, we must look outside Mexico to find a market price. In the case of heavy fuel oil, PEMEX sells for export to foreign purchasers at a free market price equivalent to the price at which fuel oil is sold in most world markets. In effect, we can say that the Government of Mexico gives its domestic industries a discount from that export market price; and the amount of that discount is the true value of the subsidy.

The first alternative under consideration today--measuring the amount of subsidy as the difference between the controlled domestic price and the export price--would provide an excellent measure of the true value of subsidies like the Mexican fuel oil subsidy. There may be other measures, such as the price on world markets, that would provide an equally fair and predictable benchmark. Indeed, there is something to be said for specifying alternative measures of the fair value price.

For example, the legislation might require the ITA to look first to the export price. In the event that there was no arm's-length export price for a natural resource product from Mexico or from some other country under investigation, then the ITA could refer to prices on world markets. In most cases, as with fuel oil, export prices of natural resource products are fairly consistent around the world. Alternatively, if there were no ascertainable arm's-length world price, the ITA could refer to the price generally available in arm's-length transactions to U.S. producers, because that price would be the best available benchmark for compensating U.S. companies for the unfair advantage provided by the foreign subsidy.

In some ways, this would be similar to the second approach being considered by the Subcommittee, which would impose duties equal to the difference between the controlled price and the lower of (1) the export price or (2) the price generally available to U.S. producers. However, we believe that the purpose of countervailing duties should be to counteract the <u>full amount</u> of any preferential pricing. If the countervailing duty were measured only by the U.S. price, then foreign governments with high natural resource costs would be able to subsidize their industries by providing them with natural resources at prices artificially low for the foreign country's market, but not lower than the competitive U.S. market price, thus nullifying the U.S. firms' natural competitive advantage. We therefore believe that the U.S. price would be a less reliable benchmark than export or world market price, and should be used only if no export or world market price exists.

We respectfully disagree with the Subcommittee's third alternative approach, which we understand is partly based on H.R. 4015, which was introduced on September 28 by Rep. Moore.[*] The Subcommittee version would have the ITA set a countervailing duty after assessing four factors: (a) the generally available world price, (b) the average price to U.S. producers, (c) production costs and the extent to which they bear a reasonable relationship to the world price, and (d) the degree of price suppression in the domestic market caused by the government regulation. First, a subjective "assessment" of qualitative "factors" would not provide the precision and certainty necessary for computing countervailing duties. Countervailing duties must be based on objective fact, not subjective balancing of different "factors."

---

[*] In fact, we agree with the general approach taken by H.R. 4015, and believe that that bill, with comparatively minor technical changes, would provide much the same relief as the proposals before this Subcommittee. Our principal disagreement with H.R. 4015 is limited to the subsidy benchmark issue, and is the same as our disagreement with the Subcommittee's third alternative approach.

Second, production costs have nothing to do with the benefit provided to companies that have access to subsidized oil. The "cost" to the Government of Mexico of producing oil from government-owned reserves may be quite low in relation to that oil's true market value. But the amount of subsidy provided by selling that oil at a preferential price is the difference between that price and the free market value, the price that the customer would have had to pay if the government had not sold the oil at a bargain price. You determine that market value by looking at the arm's-length price on some free market, such as the export market or the world market. You don't do it by looking at cost of production.

Third, factor "d," "the degree of price suppression in the domestic market caused by the government regulation," is simply too vague. In effect, it says "the countervailing duty should equal the amount of the subsidy," but does not explain how to measure the subsidy. When the foreign government controls its domestic market, the only way to determine a competitive price level is to refer to some competitive market, such as the export market, the world market, or the U.S. market. Anything else would be pure speculation. We believe that the proposed legislation should be objective, rather than speculative, and should state as precisely as possible how the countervailing duty shall be calculated.

In summary, Mr. Chairman, we believe that the proposed legislation addresses a problem of great importance to many American industries. To be effective, we believe that the legislation should rely on a simple and accurate measure of the fair value of the resource being subsidized, such as export price or world market price. Only if such a standard is in place and enforced will American companies be able to compete on a fair and equal basis with foreign companies whose natural resource costs are almost completely eliminated by government action.

Chairman GIBBONS. Thank you, Mr. Bronson. That is a fine statement.

Mr. Samuel Coco, please.

STATEMENT OF SAMUEL B. COCO, JR., SENIOR VICE PRESIDENT, CABOT CORP.

Mr. COCO. Thank you, Mr. Chairman.

I am Samuel B. Coco. I am senior vice president of Cabot Corp., responsible for the Performance Chemicals Group.

Cabot is a 100-year-old manufacturing company with annual sales of about $1.6 billion. Approximately one-third of those sales come from our oldest business, the manufacture of carbon black.

I appreciate having the opportunity to express our view that foreign subsidies—in the form of two-tier pricing on petroleum-based raw materials—should be countervailable under U.S. trade law. Of the three alternatives for measuring the subsidy under consideration today, we favor the one that would measure the difference between the controlled domestic price of the petroleum-based raw material and the fair market value for that material; we believe this is a workable compromise for U.S. petrochemical producers.

Let me provide you with some background on our industry and why we are concerned with the current trade law interpretation.

Carbon black has become an indispensible material in the modern world; it is many things—a pigment, a reinforcing agent in rubber, an electricity conductor and a material resistant to ultraviolent light. Carbon black is critical in tires and other automotive parts, printing inks, computers, and farming.

Cabot producing 2 billion pounds of this specialty chemical annually, which represents nearly 25 percent of the free world capacity. We have four carbon black plants in the United States; one each in Texas and West Virginia and two in Louisiana. These domestic operations employ about 800 people.

As the oldest continuous producer of carbon black, Cabot is committed to manufacturing the highest quality of carbon black for the lowest cost. We have invested millions of dollars in the last decade to make our plants energy efficient and to advance our product development and process technology—so that we can be the low-cost producer.

This is particularly important, not just because it makes good business sense but because the carbon black industry is a troubled one. It is currently suffering from a 20-percent overcapacity despite the fact that six U.S. plants with a total capacity of 952 million pounds of product have closed in the last 3 years. Some U.S. companies are selling or trying to sell their carbon black businesses because they are not profitable enough. There is great price competition in the industry—comparable to the gasoline wars of the 1950's and 1960's.

While these economic conditions have been in evidence for the last several years, they are being exacerbated by unfair trading policies which allow foreign governments to undercut U.S. producers.

Last November, Cabot asked the U.S. Department of Commerce to impose a countervailing duty on carbon black imports to the United States from Mexico. During its investigation of our petition, the International Trade Administration, ITA, found that Mexico was subsidizing its producers of carbon black in a number of ways.

Specifically, they found that Mexico was selling carbon black feedstock, the principal petroleum-based raw material from which carbon black is made, to Mexican producers for less than $2 per barrel, while an equivalent barrel sold to U.S. producers cost $26 per barrel. Since petrochemical feedstocks represent 70 percent of the cost of producing carbon black, Mexican producers are operating with a giant cost advantage.

Despite these numbers, the ITA found that Mexico's feedstock subsidy was not countervailable because current U.S. law does not protect U.S. industry from subsidies which foreign countries make generally available to its local industries.

However, there are only two carbon black producers in Mexico: One owned by Pemex, Mexico's Government-controlled oil company; the other is partly owned by a Government-managed financial institution. Since only these two companies have any use for carbon black feedstocks, Cabot does not believe it is generally available.

The Mexican subsidy of feedstock prices are significant and damaging; let me put the numbers into perspective. Based on a $26 barrel of feedstock, a U.S. producer is paying 13 cents to 16 cents in raw material costs for each pound of carbon black he produces; a Mexican producer with a $2 barrel of feedstock is paying only 1 cent for the raw material in a pound of his product. This 12-cent to 15-cent advantage is equal to 50 percent or more of the average price of a pound of carbon black.

In a low-margin business, this kind of cost advantage cannot be offset through technological advance or efficient operations. In fact, if U.S. producers decided to write off all the costs of production and simply charge for carbon black what they pay for feedstock alone, they still could not compete with the subsidized price of Mexican carbon black.

In fact, today Mexican producers are offering their product in the United States at 1 cent less per pound than whatever the going rate for the product and by so doing, they are unfairly manipulating the U.S. market.

It is important for you to know that this low-cost feedstock was intentionally not made available to non-Mexican carbon black producers such as Cabot. If the Mexicans simply want dollars to repay American bankers, they could sell their feedstock directly to American carbon black producers. Cabot would gladly pay the world price for this feedstock.

Of importance to you here today is the fact that Mexico has announced plans to expand its carbon black capacity and has said that this additional production would be exported to the United States. Such action would follow on the heels of continually increasing imports of carbon black from Mexico. Just a few days ago, Chemical Week magazine reported that Hules-Mexicanos, one of the Mexican producers, will export to the United States 22 million pounds of carbon black this year—up 228 percent from last year—and expects to increase that amount to 92 million pounds in 1984.

Ninety-two million pounds is the equivalent of the annual output of an average carbon black plant in the United States and is a 318-percent increase over 1983. Since there is more than enough domestic carbon black to satisfy current demand, the only way the Mexicans can increase their sales this significantly is by continuing to undercut U.S. and world prices.

Clearly, by ignoring the subsidy on carbon black feedstock, the ITA has emboldened Mexico. If these subsidies continue to be ignored, foreign producers with Government-subsidized raw materials will capture larger and larger shares of the U.S. carbon black market and more of our own plants will close.

I want to thank you for recognizing that U.S. trade laws should be modified to remedy the unfair foreign advantage that currently exists and want to emphasize that we believe the subsidy should be measured as the difference between the controlled domestic price and the fair market value. While determining the fair market value is more difficult for some materials, for carbon black, using the generally available world price or the price generally available to U.S. producers in current markets would be both straightforward and equitable.

Thank you, Mr. Chairman.

Chairman GIBBONS. Thank you.

Mr. McCoy, I am sorry I overlooked you on the list. You are next.

STATEMENT OF JON McCOY, PRESIDENT, VALLEY BUILDERS SUPPLY CO.

Mr. McCOY. That is all right, Mr. Chairman.

My named is Jon McCoy. I am president of Valley Builders Supply of Pharr and San Benito, Tex.

We are in the business of manufacturing and marketing concrete block, cement brick and related masonry products. Our company, which has been in the block manufacturing business since 1940, employs 60 people and operates 3 manufacturing facilities. Our plants are among the most modern and efficient in the United States.

I'm a small businessman. I don't know much about international trade law, but I do know that my business and my employees' jobs are being destroyed by subsidized Mexican imports. I'm speaking to you today as a last resort not only for my own company, but also on behalf of many other affected companies in four States—California, New Mexico, Arizona, and Texas—and the National Concrete Masonry Association.

Notwithstanding our modern production facilities, our company is being devastated by sales losses to Mexican concrete block imports. Our block sales declined by an estimated 60 percent from 1981 to 1983. Without relief, we will not be able to continue to employ our workers or to operate our company.

There is no way we can compete with the Mexican imports. The primary reason is very simple—it is the cost of oil and gas as set by the Mexican Government for producers in Mexico versus the market cost of energy that I must pay in the United States.

Our direct cost of production is about 75 cents per block. Our Mexican counterparts are selling block in our market area for 37-65 cents per blocks.

The artificial energy pricing advantage enjoyed by Mexican producers of concrete block hits us at two levels. First, the concrete block manufacturing process itself is energy intensive. About 33 percent of my total direct cost of producing and delivering concrete block is the cost of energy.

Second, the manufacturing processes used in making the raw materials for producing block are even more highly energy intensive. The two basic raw materials used in the production of block are cement and aggregate. The principal cost of producing each is energy. I have to pay $77.60 per ton for the cement I purchase. My competitors in Mexico are paying $39 per ton.

The energy portion of our direct manufacturing and delivery costs is about 33 cents per block, and the natural gas cost of manufacturing just the aggregate that we use in producing block is another 21 cents, for a total of 54 cents. The energy portion of the cost of manufacturing cement must be added as well. Thus, in many instances the Mexican cement imports with which we must compete are being sold for less than the energy portion alone of our cost of manufacturing block and our suppliers' cost of producing the raw materials we use in making block.

The artificial cost advantage enjoyed by the Mexican block producers is so great that they are able to penetrate markets far from the Mexican border in which they otherwise could not compete. Our company is limited to no more than a 120-mile market area because of transportation costs. Because of the energy subsidy, the Mexican producers are able to haul from Monterrey, Mexico, to San Antonio and Houston—a distance of nearly 500 miles, Mr. Chairman—and remain below the competing prices of local producers in those areas.

I ask the subcommittee to give us the chance to compete on equal terms with our Mexican counterparts by amending the law to recognize that when a government provides oil or natural gas at far less than its market value, that is a subsidy and that such a subsidy should be countervailable. Moreover, it should be countervailable not only when it is provided to the manufacturers of goods exported to the United States, but also when it is provided to the producers of materials used in manufacturing goods exported to this country.

Gentlemen, I thank you for allowing me to appear before you today and I implore you to act to provide us relief from this unfair and damaging practice.

Thank you.

[The prepared statement follows:]

STATEMENT OF JON McCOY, PRESIDENT OF VALLEY BUILDERS SUPPLY CO.

My name is Jon McCoy. I am President of Valley Builders Supply, Inc. of Pharr and San Benito, Texas. We are in the business of manufacturing and marketing concrete block, cement brick and related masonry products. Our company, which has been in the block manufacturing business since 1940, employs 60 people and operates three manufacturing facilities. We utilize the latest technology in our manufacturing process. Our plants are among the most modern and efficient facilities in the United States.

I am speaking today not only for my own company, but also on behalf of many other affected companies in four states—California, New Mexico, Arizona, and Texas—and the National Concrete Masonry Association—an association composed of 800 member companies worldwide.

Notwithstanding our modern production facilities, our company is being devastated by sales losses to Mexican concrete block imports. Our block sales declined by an estimated 60 percent from 1981 to 1983. We literally are faced with a do or die situation. Without relief, we will not be able to continue to employ our workers or to operate our company.

There is no way we can compete with the Mexican imports. The primary reason we cannot is very simple to understand—it is the cost of energy as set by the Government in Mexico versus the market cost of energy that I must pay in the United States.

The artificial energy pricing advantage enjoyed by Mexican producers of concrete block hits us at two levels. First, the concrete block manufacturing process itself is energy-intensive. About 33 percent of my total direct cost of producing and delivering concrete block is the cost of energy—the natual gas and electricity used in our production process and the diesel fuel used in delivering our finished product.

But even more importantly, the manufacturing processes that are used in making the raw materials we use in producing block are even more highly energy-intensive. The two basic raw materials other than water used in the production of block are cement and aggregate. It is my understanding that the principle cost of producing cement is energy. I have to pay $77.60 per ton for the cement I purchase. One of my competitors in Mexico has told me that he pays $39 per ton for cement—less than I believe it costs United States cement companies to manufacture a ton of cement.

It takes more than $15 worth of natual gas alone to produce one yard of lightweight aggregate—more than half of its cost of production. With that one yard of aggregate we are able to produce 72 concrete blocks. This means that we have a cost of 21 cents per block for the natural gas used in producing the aggregate used in the block alone. This cost does not include the other production costs, overhead or profit of our aggregate supplier or the cost of freight.

Our direct cost of production is about 75 cents per block. Our Mexican counterparts are selling block in our market area for 37–65 cents per block, depending on what the market will bear. That price includes production, transportation, overhead and profit.

The energy portion of our direct manufacturing and delivery costs alone is about 33 cents per block, and the natural gas cost (alone) of manufacturing just one raw material we use in producing block—aggregate—is another 21 cents, for a total of 54 cents. The energy portion of the cost of manufacturing cement must be added as well. Thus, in many instances the Mexican cement imports with which we must compete are being sold for less than the energy portion alone of our cost of manufacturing block and our suppliers cost of producing the raw materials we use in making block.

The artificial cost advantage enjoyed by the Mexican block producers is so great that they are able to penetrate markets far from the Mexican border in which they otherwise could not compete. Our company is limited to no more than a 120 mile market area because of transportation costs. We cannot haul to San Antonio or

Houston and remain competitive. Because of the energy subsidy, the Mexican producers are able to haul from Monterrey, Mexico to San Antonio and Houston—a distance of nearly 500 miles—and remain below the competing prices of local producers in those areas.

If conditions stay as they are, I will have no choice but to shut down my operations and lay off my employees.

I ask the Subcommittee to give us the chance to compete on equal terms with our Mexican counterparts by changing the law to recognize that providing energy at far less than its market value is a subsidy and that such a subsidy should be countervailable not only when it is provided to the manufacturers of goods exported to the United States, but also when it is provided to the producers of materials used in manufacturing goods exported to this country and is reflected in the price of those goods.

Gentlemen, I thank you for allowing me to appear before you today and I implore you to act to provide relief from this unfair and damaging practice.

Chairman GIBBONS. Thank you, sir.

Our last witness on this panel is Mr. Newhouse of Hammond Lead Products.

STATEMENT OF EDGAR NEWHOUSE, COUNSEL, ON BEHALF OF WILLIAM P. WILKES, PRESIDENT, HAMMOND LEAD PRODUCTS, INC.

Mr. NEWHOUSE. Mr. Chairman, members of the committee, and staff, my name is Edgar Newhouse, I have represented Hammond Lead Products, Inc., since 1976. I have been asked by the president of that company to present his statement at this hearing.

Hammond Lead Products, Inc., is a major producer of lead oxides, commonly known as litharge and red lead. We have been in business since 1931 and operate two plants in Hammond, Ind., and one in Pottstown, Pa.

Lead oxides are manufactured by a process of oxidizing refined lead which we obtain for the most part from U.S. producers of primary lead.

Lead oxides are employed in battery manufacture, special glass production, the ceramics and electronic parts industry, the plastics industry, and as protective coatings, as well as in a number of other diversified uses, including certain defense products.

Since 1958, the U.S. lead oxide industry has suffered greviously from imports of Mexican lead oxides largely as a result of a two-tier pricing system for lead in Mexico. Imports from other countries have been negligible.

Until recently no administration has seen fit to give this problem any constructive attention. Quite the contrary.

For example, in 1958, when the U.S. imposed quotas on refined lead, no quotas were imposed on finished products containing lead; consequently, lead oxide imports from Mexico rose from 8,000 tons in 1958 to 22,000 tons by 1965.

Moreover, in 1970 the administration appealed a U.S. Customs Court unanimous decision which had found in favor of Hammond Lead in a countervailing duty case which we had brought as a result of the Mexican two-tier price practice. As a result of the appeal this decision was overturned on a jurisdictional basis.

Chairman GIBBONS. Let me get the dates in my mind.

When did you bring the case? Let me get the dates because they bear on this whole discussion.

Mr. NEWHOUSE. We brought this case before the U.S. Customs Court in 1968.

Chairman GIBBONS. Alleging then that a two-tiered pricing system—1968?

Mr. NEWHOUSE. Yes, sir.

Chairman GIBBONS. Alleging that a two-tiered pricing system was countervailable?

Mr. NEWHOUSE. Yes, sir.

Chairman GIBBONS. The Customs Court agreed unanimously with you?

Mr. NEWHOUSE. Yes, sir.

Chairman GIBBONS. When was that decision made?

Mr. NEWHOUSE. The decision came in 1969.

Chairman GIBBONS. 1969. All right. And you got reversed on it, on a procedural basis?

Mr. NEWHOUSE We got reversed on a jurisdictional basis. The U.S. Court of Customs and Patent Appeals found that the U.S. Customs Court did not have jurisdiction. That decision was due to an appeal made by the administration.

Chairman GIBBONS. OK. When was that reversal made?

Mr. NEWHOUSE. In 1970.

Chairman GIBBONS. Thank you,

Mr. NEWHOUSE. Were this not enough, in 1979, as part of the multilateral trade negotiations, the United States agreed with Mexico to reduce the U.S. duty on lead oxide—litharge—from a base of 6 percent ad valorem to 2.4 percent ad valorem on condition that Mexico join GATT. This concession was totally unwarranted in that it established a rate of duty on a finished product that was below the duty on its raw material, lead. When Mexico refused to join GATT, the Office of the Special Trade Representative refused to roll back the duty on litharge to 6 percent ad valorem and agreed with Mexico on a duty of 3 percent, the same as that for unwrought lead.

STR gave the incredible excuse that Mexico had agreed to bind its duties on aluminum products of which it has only limited production and, therefore, was entitled to a concession. This obviously, in our opinion, Mr. Chairman, was a political decision.

The only relief that has occurred came in 1982 when the Department of Commerce found for a countervailing duty of 3.73 percent ad valorem on litharge, red lead and lead stabilizers as a result of a Mexican preferential financing program known as Fomex.

This countervailing duty, while it affords some small help, does not address the principal problem which is the two-tier pricing system in Mexico. This system makes it possible for Mexican producers of lead oxide to purchase their raw material—lead—at a weekly Mexican Government price known as the Boletin price which has been substantially below the world price and the U.S. producer price.

In 1968 the situation with respect to lead pricing in Mexico was as follows: Mexican refined lead sold for export at a price which included an export tax; Mexican refined lead sold to Mexican manufacturers of lead products such as lead oxides, did not include the export tax. Moreover, lead oxides were not subject to export taxes as were other lead products. This allowed the Mexican exporter of lead oxides to retain the price advantage received upon his acquisition of refined lead. Given these facts, the U.S. Customs Court in 1969 as the result of a countervailing duty suit brought by Hammond Lead found that the Mexican practices constituted a bounty and rendered a unanimous decision in favor of Hammond Lead.

As has been previously stated, this decision was overturned by the U.S. Court of Customs and Patent Appeals in 1971 on the basis of jurisdiction. The matter of jurisdiction, however, was settled in the Trade Agreement Act of 1974 which gave the U.S. Customs Court jurisdiction in countervailing duty cases.

At about this time, fearing that Hammond Lead would institute another countervailing duty case the Government of Mexico made certain changes in their tax practices. A production tax on refined lead was substituted for the export tax. Export taxes on most lead products were removed. These changes, however, had little effect on the two-tier pricing system. Mexico continues to publish a weekly Boletin price for lead which is the maximum price available for Mexican producers of lead products such as litharge and red lead, and is well below the U.S. and world price.

The average yearly differences between the Boletin price of lead and the U.S. producer price of lead in cents per pound varied from 3 cents to 5 cents per pound from 1976 to 1983. While we have given only the yearly differences, an examination of weekly and monthly differences between the Boletin price and the U.S. producer price shows the disparity at times has been as high as 10 cents per pound.

Mexican lead at the Boletin price is not available for export from either of the two Mexican producers, although counsel for the lead oxide producers in Mexico would have us believe otherwise. Mexican refined lead for export to the United States is sold at only a very small discount off the U.S. producer price.

The two-tier price system in Mexico has had a serious impact on the U.S. lead oxide industry. Three of the largest U.S. producers have, over the last 5 years, gone out of the business as the Mexican producers have consistently been able to undercut the U.S. price of lead oxides by as much as $50 per ton or more on occasion.

In the case of Hammon Lead, we pride ourselves on the fact that we have installed the most modern cost-effective equipment available for the manufacture of lead oxides yet we are unable to meet Mexican competition. Moreover, we are subject to more stringent environmental controls than any that have been required in Mexico. We are not alone in this dilemma as witnessed by the fact that other countries have been faced with the same problem as evidenced by their tariffs on lead oxides which they have been forced to impose.

These tariffs are as follows: United Kingdom, 12 percent ad valorem; European Economic Community, 11.8 percent; Canada, 14.4; Japan, 10.2.

Hammond Lead Products, Inc., seeks no more than an opportunity to compete with Mexican producers of lead oxides on a fair basis. The unnatural trade advantage as a result of the two-tier pricing system has been exploited by the Mexicans at the expense of the U.S. lead oxide industry for many years. This committee and you, Mr. Chairman, are to be commended for your initiative in seeking to address ways and means for correcting the results of this unfair pricing system and my company stands ready to assist your committee in this endeavor in any way.

[The prepared statement follows:]

STATEMENT OF WILLIAM P. WILKES, PRESIDENT, HAMMOND LEAD PRODUCTS, INC., HAMMOND, IND.

Hammond Lead Products, Inc. is a major producer of lead oxides, commonly known as litharge and red lead. We have been in business since 1931 and operate two plants in Hammond, Indiana and one in Pottstown, Pennsylvania.

Lead oxides are manufactured by a process of oxidizing refined lead which we obtain for the most part from U.S. producers of primary lead.

Lead oxides are employed in battery manufacture, special glass production, the ceramics and electronic parts industry, the plastics industry, and as protective coatings, as well as in a number of other diversified uses, including certain defense products.

Since 1958, the U.S. lead oxide industry has suffered grievously from imports of Mexican lead oxides largely as a result of a two-tier pricing system for lead in Mexico. Imports from other countries have been negligible.

Until recently no Administration has seen fit to give this problem any construction attention. Quite the contrary.

For example, in 1958, when the U.S. imposed quotas on refined lead, no quotas were imposed on finished products containing lead; consequently, lead oxide imports from Mexico rose from 8,000 tons in 1958 to 22,000 tons by 1965.

Moreover, in 1970 the Administration appealed a U.S. Customs Court unanimous decision which had found in favor of Hammond Lead in a countervailing duty case which we had brought as a result of the Mexican two-tier price practice. As a result of the appeal this decision was overturned on a jurisdictional basis.

Were this not enough, in 1979, as part of the multilateral trade negotiations, the U.S. agreed with Mexico to reduce the U.S. duty on lead oxide (litharge) from a base of 6 percent ad valorem to 2.4 percent ad valorem on condition that Mexico join GATT. This concession was totally unwarranted in that it established a rate of duty on a finished product that was below the duty on its raw material (lead). When Mexico refused to join GATT, the Office of the Special Trade Representative refused to roll back the duty on litharge to 6 percent ad valorem and agreed with Mexico on a duty of 3 percent, the same as that for unwrought lead. STR gave the incredible excuse that Mexico had agreed to bind its duties on aluminum products of which it has only limited production and, therefore, was entitled to a concession. This obviously was a political decision.

The only relief that has occurred came in 1982 when the Department of Commerce found for a countervailing duty of 3.73 percent ad valorem on litharge, red lead and lead stabilizers as a result of a Mexican Preferential Financing Program known as Fomex.

This countervailing duty, while it affords some small help, does not address the principal problem which is the two-tier pricing system in Mexico. This system makes it possible for Mexican producers of lead oxide to purchase their raw material (lead) at a weekly Mexican Government price known as the "Boletin Price" which has been substantially below the world price and the U.S. Producer Price.

In 1968 the situation with respect to lead pricing in Mexico was as follows: Mexican refined lead sold for export at a price which included an export tax; Mexican refined lead sold to Mexican manufacturers of lead products such as lead oxides, did not include the export tax. Moreover, lead oxides were not subject to export taxes as were other lead products. This allowed the Mexican exporter of lead oxides to retain the price advantage received upon his acquisition of refined lead. Given these facts, the U.S. Customs Court in 1969 as a result of a countervailing duty suit brought by Hammond Lead found that the Mexican practices constituted a bounty and rendered a unanimous decision in favor of Hammond Lead. As has been previously stated, this decision was overturned by the U.S. Court of Customs and Patent Appeals in 1971 on the basis of jurisdiction. The matter of jurisdiction, however, was settled in the Trade Agreement Act of 1974 which gave the U.S. Customs Court jurisdiction in counter-vailing duty cases.

At about this time, fearing that Hammond Lead would institute another countervailing duty case the Government of Mexico made certain changes in their tax practices. A production tax on refined lead was substituted for the export tax. Export taxes on most lead products were removed. These changes, however, had little effect on the two-tier pricing system. Mexico continues to publish a weekly "Boletin" price for lead which is the maximum price available for Mexican producers of lead products such as litharge and red lead, and is well below the U.S. and world price. The following table is illustration of this fact:

Average yearly difference between Boletin price and U.S. producer price in cents per pound

1976	5.13
1977	4.35
1978	5.00
1979	3.31
1980	3.03
1981	5.07
1982	3.66
1983 (January to August)	3.72

It is of interest to note that there is no production tax on lead oxides and that exports of lead products other than lead oxides are minimal. Whether or not the Mexican practice still constitutes a bounty under the present U.S. countervailing duty statute remains to be seen.

While we have given only the yearly differences in the foregoing table, an examination of weekly and monthly differences between the Boletin Price and the U.S. Producer Price shows the disparity has been as high as 10.00 cents per pound.

Mexican lead as the Boletin Price is not available for export from either of the two Mexican producers, although counsel for the lead oxide producers in Mexico would have us believe otherwise. Mexican refined lead for export to the U.S. generally is sold at only a very small discount off the U.S. Producer Price.

The two-tier price system in Mexico has had a serious impact on the U.S. lead oxide industry. Three of the largest U.S. producers have, over the last five years, gone out of the business as the Mexican producers have consistently been able to undercut the U.S. price of lead oxides by as much as $50 per ton or more on occasion.

In the case of Hammond Lead, we pride ourselves on the fact that we have installed the most modern cost effective equipment available for the manufacture of lead oxides yet we are unable to meet Mexican competition. Moreover, we are subject to more stringent environmental controls than any that have been required in Mexico. We are not alone in this dilemma as witnessed by the fact that other countries have been faced with the same problem as evidenced by their traiffs on lead oxides which they have been forced to impose. These tariffs are as follows:

United Kingdom—12 percent CIF value; European Economic Community—11.8 percent CIF value; Canada—14.4 percent FOB SP value; and Japan—10.2 percent CIF value.

Hammond Lead Products, Inc. seeks no more than an opportunity to compete with Mexican producers of lead oxides on a fair basis. The "unnatural trade advantage" as a result of the two-tier pricing system has been exploited by the Mexicans at the expense of the U.S. lead oxide industry for many years. This Committee and you, Mr. Chairman, are to be commended for your initiative in seeking to address ways and means for correcting the results of this unfair pricing system and my company stands ready to assist your committee in this endeavor in any way.

Chairman GIBBONS. Thank you.

I will depart from the prepared script now and ask Mr. Rivers to come forward.

Would you come forward, Mr. Rivers, and take the microphone?

Mr. Rivers, I am asking you to be a witness today because I recognize that you are unique in our historical pattern around here. You were the negotiator of many of these matters.

I don't want to overpaint your position. Maybe you can tell me, refresh my memory, and for the record, tell me where you stood in your employment during the time that the MTN was being negotiated and comment on some of these matters we are going into today.

When you get through that, I will ask you specifically whether or not you think what the committee has been proposing here is a violation of the letter or spirit of the MTN or of the Subsidies Code or the GATT. So you are forewarned. Go forth.

STATEMENT OF RICHARD R. RIVERS, ESQ., AKIN, GUMP, STRAUSS, HAUER & FELD, WASHINGTON, D.C.

Mr. RIVERS. Thank you, Mr. Chairman.

My credentials are that in the early years of the Tokyo round I was a professional staff member on the Senate Finance Committee, as you know.

Chairman GIBBONS. On the Senate side, yes.

Mr. RIVERS. Later, I served as general counsel in the Office of the Special Trade Representative for a period of almost 3 years, early 1977 through 1979. In that capacity, I was the head of the team that negotiated the Subsidies Code in behalf of the United States.

Your question is, Does the proposal that the subcommittee presently has before it violate the GATT or the Subsidies Code?

I think Mr. Gingrich's answer, insofar as I understood it, was substantially correct. The basic principle under the GATT is that any government may take an action to offset foreign practices that are causing injury to its domestic producers.

Neither the GATT nor the Subsidies Code or even the U.S. countervailing duty statute contain a definition of the word "subsidy." Congress and the executive branch have scrupulously avoided a strict definition of the term "subsidy" for a number of reasons, not the least being that any definition could be easily evaded.

Accordingly, in my opinion there is nothing in the GATT or the Subsidies Code that would preclude the United States from recognizing that a two-tiered energy pricing system can constitute a form of subsidization and from using any reasonable basis for measuring that subsidization.

At the outset, it is up to us. Now, although the GATT does not contain a definition of subsidy, it does in article 16 contain some interesting language imposing an obligation on a government to notify the GATT if it, and I quote, "grants or maintains any subsidy, including any form of income or price support"—I wish to emphasize this—"which operates directly or indirectly to increase exports of any product from, or reduce imports of any product into, its territory."

There is no question that the two-tiered pricing scheme presently in place in Mexico operates to increase exports.

In addition, the Subsidies Code contains, as you know, an annex which is an illustrative list of prohibited export subsidies which is based on work that was begun in the GATT in the 1960's.

This illustrative list contains an interesting example of how governments can provide subsidies in the form of goods or services such as natural gas, for example, at concessional prices and thereby create an export subsidy.

The language I refer to is paragraph D in the prohibited export subsidy list and I would like to read that briefly, if I may.

The language reads:

> The delivery by governments or their agencies of imported or domestic products or services for use in the production of exported goods, on terms or conditions more favorable than for delivery of like or directly competitive products or services for use on the production of goods for domestic consumption, if—in the case of prod-

ucts—such terms or conditions are more favorable than those commercially available on world markets to its exporters.

The Mexican two-tiered price system doesn't exactly fit that definition. That is not exactly it.

But it is not too far from it either. Mexico has in fact designed a system to build a petrochemical industry which is aimed, in its own words, at foreign markets. It may not constitute an export subsidy strictly speaking, but it is certainly subsidy on products exported from Mexico if you understand the distinction I make.

The fact is that Mexico's production subsidy is neither fish nor fowl. It doesn't neatly fall into any of the pat pigeonholes that U.S. trade policy attempts to place subsidy practices in.

Ultimately, whether or not Congress decides that it regards this as a subsidy practice, that is entirely up to the United States. What we may decide is a subsidy practice may not be agreed to by other countries. In that event they can take the issue up in the Subsidies Code Committee or indeed the GATT Council.

That is the way the system is designed to work. For example, the European Community right now is contesting the Department of Commerce's calculation of subsidies in the steel cases in the Subsidies Code Committee. Those talks are going forward right now in Geneva and it is through this international process that we will arrive at over time an international consensus on what subsidies are and how they ought to be measured.

That is the way the system is supposed to work.

Chairman GIBBONS. Thank you.

Mr. RIVERS. That was not brief, but this is not an easy subject.

Chairman GIBBONS. I realize it is not an easy subject and I appreciate your unique expertise in this matter based on your official position in the Congress and your STR position and your unique position in having negotiated the code.

Let me go back to have the record as clear as it can possibly be, is what we are proposing to do here a violation of the letter or the spirit of the GATT or the Subsidies Code?

Mr. RIVERS. No, sir. In my opinion, it is not.

Chairman GIBBONS. I don't know of anybody that is a better expert than you. Thank you very much.

I want to thank all the panel. Your testimony has been excellent and I want to make—excuse me. Mr. Russo.

Mr. RUSSO. Mr. Chairman, I would like to ask a question of Mr. Gerstell and any other member of the panel who wishes to respond.

I understand the problem which you face with the low energy cost as a result of the Mexican Government's two-tier pricing system. I want to know how much cooperation you had with the Department of Commerce and with this administration dealing with this problem on a bilateral basis with the Mexican Government.

Mr. GERSTELL. Well, Mr. Russo——

Mr. RUSSO. Was there any cooperation or not?

Mr. GERSTELL. Congressman, I think the answer to that is that we have been in contact with the Commerce Department from the moment this problem arose and began to have a negative impact on us. We would not be here today if we had gotten any satisfactory solution to the problem, sir.

Mr. RUSSO. Let me ask you this. In your discussions with them and dealing with them and trying to resolve the problem with the Mexicans, did they offer any other ideas or remedies you could use that would be helpful in dealing with this problem?

Did they suggest any alternative like, as Mr. Frenzel said, he asked a question of one of the Commerce Department, did they file a 201 case in a particular situation. Were they helpful in giving you other ideas in areas where maybe the request would move quickly and you would be more successful and address the injury quicker?

Mr. GERSTELL. As you know, we did get a 5.6-percent duty imposed but that is not satisfactory. I am not—I can't recall any specific innovative ideas put forth for our consideration.

Mr. RUSSO. You are on your own once you deal with Commerce, you have to come up with the ideas, you have to file the things and they will just investigate. They don't offer any assistance or help to you at all, other than just doing their job under the statute, I guess?

Mr. GERSTELL. We don't overlook the Commerce Department, Congressman. They are an agency, an administrative arm that we do depend on, but, no, we foresee no other——

Mr. RUSSO. The point I am trying to make is that in my discussion with them earlier they talked about wanting to be helpful in trying to remedy the loss. They are more experienced at what would move quickly through the Commerce Department to deal with the situation than any individual such as yourself going there to file it.

My concern is are they treating our American companies in such a way saying this is not a good idea, you ought to file this or that because you will move quicker in that area.

Mr. GERSTELL. They did not respond to our needs, Congressman, and we hope this committee will.

Mr. RUSSO. That is the bottom line. That is why you are here. Thank you, Mr. Chairman.

Chairman GIBBONS. I want to thank all the panel members for coming here today. Your statements have been illuminating and I would not want anybody reading this record at this point to believe that this is just a hearing on cement or carbon black or lead or a group of products like that or even on petroleum or natural gas. This is a problem of subsidies we are talking about here. As I have stated so many times, I am a free trader, but subsidized trade is not free trade. It is distorted trade. It is one of the growing forms of protectionism—subsidized trade.

It is my objective—and I believe the objective of the great majority of the members of this committee—to level the playing field and to get rid of the distortions. That means getting rid of the subsidies. Now, subsidies that do not impact upon us are none of our business, and subsidies that probably only lightly impact upon us and are not injurious to us are not a concern of government. But when subsidies become so onerous that they injure us, under the definition in the General Agreement on Tariffs and Trade and the Subsidies Code, then they are our business. They are our highest business. Thank you very much for coming.

We will have a panel now for the Cargill Corp., Mr. Robbin Johnson, vice president for public affairs; Edwin Wheeler, president, Wheeler & Associates; and the National Grange, National Association of Wheat Growers, Robert Hampton, representing Edward Anderson.

Mr. Johnson, would you go ahead.

STATEMENT OF ROBBIN JOHNSON, VICE PRESIDENT FOR PUBLIC AFFAIRS, CARGILL, INC., ACCOMPANIED BY KEN SCHUSTER

Mr. JOHNSON. Thank you, Mr. Chairman. I appreciate this opportunity to discuss the complex, important issue of upstream subsidies. I have a prepared text that I will submit for the record and will summarize that statement.

Chairman GIBBONS. Fine.

Mr. JOHNSON. With me is Ken Schuster on my right, who is Cargill's chief nitrogen merchant. We are brought to this issue because Cargill is a domestic nitrogen manufacturer and international fertilizer merchant and involved in the domestic distribution of nitrogen and fertilizer products.

U.S. trade policy must take into account, in our judgment, our international obligations, whether remedies proposed fit the problem, and where all interests in trade are properly weighed. Cargill appears today to oppose the upstream subsidies concept as bad trade policy, unnecessary relief, and damaging to other national interests.

Let me summarize our arguments in each case.

U.S. trade policy has traditionally supported trade liberalization on the lines of comparative advantage for its general economic benefits. Part of that policy is a countervailing duty law insuring that governments do not subsidize either directly or indirectly exports that compete with U.S. producers. Proponents of the upstream-subsidies concept sought relief under that law and failed. The Commerce Department specifically found that Mexico's two-tiered pricing was not a subsidy and that the opportunity-cost test being urged on this subcommittee has no basis in law or in fact and would been totally speculative.

So, proponents of these ideas are now asking Congress to make, in our judgment, a natural cost advantage an illegal subsidy. This would be bad trade policy. Government's role in insuring a level playing field for trade covers artificial or contrived advantages, but should not extend to natural or economic advantages. Trade law historically has recognized that sovereign countries will use their resources to fit their own economic development needs and cannot be compelled to use them to fit our desires.

Since current law protects against direct subsidies or trade discrimination, the upstream-subsidies proposal looks like trade policy grounded in economic power rather than in considerations of fairness.

It should be rejected on that grounds alone. The upstream concept is unnecessary relief because imports in the nitrogen industry are largely irrelevant to the nitrogen industry's current problems. Those problems stem from powerful cyclical forces and long-term structural adjustments. Such problems are endemic to this industry. This is a vital point. Imports have not surged into the United States. New exporters have replaced traditional exporters with little change in total world trade. The Congress is asked to forge a trade solution to a nontrade problem. The U.S. nitrogen industry has seen domestic use of its product fall 25 percent since 1981. This occurred because U.S. grain exports fell 15 percent, farmers got caught in a cost-price squeeze, and PIK, the payment-in-kind program, which took 80 million acres out of production. But the nitrogen industry is not alone in its adjustment problem.

As one example, U.S. grain export elevators are currently operating at about 60 percent of capacity.

There is also a structural adjustment occurring in both the domestic and world——

Chairman GIBBONS. I understand you got plane problems, I do not want to delay you. I am not interested in all the other things. I am interested in the subsidies matter mainly. Does the rest of your statement go to anything other than the subsidies, the two-tiered pricing system? I am familiar with the nitrogen situation, the fact that farm prices are down and all that. I know about that.

Mr. JOHNSON. One essential point I want to make in that context that has not been made this morning, is that if you subtracted nitrogen imports and exports out of the nitrogen picture in the United States the problems in the domestic industry would not be materially different than they are today.

Chairman GIBBONS. I am not worried about that. I am worried about the whole picture of subsidies. That is a 201 matter or something else. It does not have anything to do with this hearing.

I am not trying the nitrogen industry or anybody else or cement industry or lead industry or anything else. This has to do with subsidies and two-tiered pricing and things like that.

I am not interested in the reasons why industries are up or down. I am just interested in subsidies. Let us talk about that.

You said that the natural cost advantages—you thought countries ought to use natural cost advantages. I do not disagree with that. But let us just take an illustration. Suppose the U.S. Government told Gulf Oil, you've got to sell your oil to Cargill to make—or say gas—to Cargill at a very low price to make nitrogen. Would you call that a natural cost advantage?

Mr. JOHNSON. If the——

Chairman GIBBONS. Natural cost advantage, I think you said natural cost advantage.

Mr. JOHNSON. I would ask the question this way, as long as Gulf Oil is covering its cost of production in that case, it would be a natural cost advantage. Gulf Oil might not have received the total economic benefit it could have from production of that natural gas, but it would not be selling it at a subsidized price. Another way of looking at a——

Chairman GIBBONS. I know it would not be selling at a subsidized price, but Cargill would be getting a heck of a good bonus somehow by Government edict. Out of Gulf's hide. I am not worried about Gulf. They got their money out of it, they got some money out of their oil. I am worried about the advantage. My illustration is this: The U.S. Government tells Gulf you got to sell your gas to Cargill way below what you could get for it anyplace else in the world, and

Cargill makes ammonia out of that. That is not a subsidy to Cargill?

Mr. JOHNSON. Well, of course we both understand the hypothetical nature of that example.

Chairman GIBBONS. It is the same thing that is happening in Mexico. Go ahead.

Mr. JOHNSON. OK.

Chairman GIBBONS. I can use that as an illustration, I just wanted to see what you would think of the subsidies to Cargill.

Mr. JOHNSON. Certainly when a country can produce a natural resource at a relatively low price and has several options in how it chooses to market it, the fact that it does not choose to market all of it in raw form at an artificially high world price but uses some of it on a nondiscriminatory and nonsubsidized basis to develop its own internal industries, I do not regard that and I do not think trade law historically or trade practice internationally regards that as a subsidy in the traditional sense of the word.

Chairman GIBBONS. We are talking about changing the law. We are not talking about what the law is.

Mr. JOHNSON. I understand.

Chairman GIBBONS. The Commerce Department told us what the law is. I am not arguing with them about that. We are talking about changing the law.

Mr. JOHNSON. In that connection I feel it is relevant to take a look at the kinds of problems that generate the request for change and the ramifications of change proposed. That was what I was trying to address in my testimony. In our judgment, at least from the nitrogen fertilizer industry perspective, the problems facing that industry are not trade related, and to forge a remedy like this which would be unusual, unique, unilateral change in practice on subsidies is highly disruptive for no obvious benefit. In agriculture we have a lot of experience with subsidized export competition, and we certainly are anxious to see that kind of unfairness dealt with directly and effectively. The problem here is that the evidence of unfair below-cost competition has not been laid on the table.

Chairman GIBBONS. You do not think the use of subsidies in the future is going to cause us problems and distortions in trade?

Mr. JOHNSON. Surely. What we are debating is what constitutes a subsidy. There is no doubt that natural resource producers that produce resources more cheaply than we will have an advantage in developing industries based on those natural resources. We are not going to be able to avoid that economic and structural adjustment. The question is, Is it occurring unfairly because of artificial policies that constitute subsidies in the normal sense of the word?

I for one would prefer to look and define subsidy as providing costs or benefits at below cost or on a discriminatory basis.

Chairman GIBBONS. Give me your definition, what you prefer again?

Mr. JOHNSON. I prefer to define a subsidy as providing a good or service below cost or on a discriminatory basis.

Chairman GIBBONS. Well, you were here when Mr. Mollohan gave the illustration of a $2 price versus a $26 price. Is that not discriminatory?

Mr. JOHNSON. As long as the $2 price covers the producer's costs, it is not discriminatory—well, two things. As long as it covers his costs it is not providing the good below its cost. And as long as the raw material is provided on the same basis to all domestic users it would not be discriminatory in the sense that it would have a distorting effect on trade.

Chairman GIBBONS. You do not believe that the difference between the discriminatory prices in what you are selling the product for is a subsidy?

Mr. JOHNSON. Well, again, Mr. Chairman, to try to turn the question around, is it discriminatory if the Mexican Government decides to withdraw from the marketing of natural gas at current world natural gas prices and decides to use all of its natural gas resources to develop its domestic industry at a price level that will cover its costs of recovering that gas?

I do not see how we would argue that that would be discriminatory or unfair or a policy that the United States——

Chairman GIBBONS. No, in fact the way I first drafted this they could do that. The way I first drafted this and the way I would prefer it, if they do not sell it at the border it does not make any difference. They do not have a price.

Mr. JOHNSON. But that is trying to deny them access to a market that is currently available. Why depart from traditional tests of——

Chairman GIBBONS. They are making—their subsidies come from the fact they are making money selling us gas that is artificially high priced and pumping it back into their local ammonia people.

Mr. JOHNSON. The returns they get from natural gas sales come about because they are able to receive that price, were able to negotiate that price with the U.S. buyer in the latter part of the 1970's.

We signed a long-term contract that at that time we regarded mutually to be beneficial. It is not a subsidy to say that they can still cover their costs while selling additional natural gas to domestic users within Mexico. The subsidy would not change if we negotiated a contract at a different price without Government policy changing at all in Mexico. We have looked at subsidy policy as governmental actions that are designed to achieve particular discriminatory effects in the past. Yet the definitions we have been looking at under the upstream-subsidies concept will have different consequences depending on developments in two different markets whether or not Government policy in Mexico changes at all.

Chairman GIBBONS. Do you have anything else you would like to add? I realize you have a plane problem.

Mr. JOHNSON. There was just one other idea that I would like to put before this subcommittee. There are a variety of interests that have to be weighed in making any kind of trade policy change.

We believe the upstream subsidies concept damages several important national interests. For one thing, it discourages developments in energy-rich countries that would advance America's interest in having reliable secure access to those energy resources. When those countries build up industry based on the development of those resources, it becomes much harder for them to shut them off. They would have to shut down industries and disrupt their economy. So we have a stake in that kind of development process.

Many of the countries that we are talking about are developing countries that already take 40 percent of U.S. exports in total and are a growth market. One of the effects of this policy to the extent it disadvantages them is going to discourage growth in export-oriented U.S. industries.

Finally, agriculture has some important concerns here. The upstream-subsidies concept shifts costs on to farmers by raising their input prices and puts U.S. farmers at a competitive disadvantage versus other exporting nations. For example, U.S. anhydrous ammonia prices swung nearly 400 percent in the last 10 years from about $80 a ton to around $300 a ton. Imports have not driven this cycle. It is endemic to the industry. Yet, the upstream subsidies concept would produce the highly undesirable result of taxing imports at every point in the cycle, including at its highest point.

That really concludes the statement I wished to make.

[The prepared statement follows:]

STATEMENT OF ROBBIN JOHNSON, VICE PRESIDENT FOR PUBLIC AFFAIRS, CARGILL, INC.

Mr. Chairman and members of the subcommittee: My name is Robbin Johnson. I am a Vice President with Cargill, Incorporated of Minneapolis, Minnesota—an international merchant and processor of agricultural and industrial commodities. With me today is Ken Schuster, Cargill's chief nitrogen merchant.

I wish to thank the chairman for this opportunity to discuss the wisdom of introducing an "upstream subsidies" concept for natural resources into U.S. countervailing duty law. The issue is important, complex and worthy of study.

An analysis of this concept with respect to the nitrogen industry leads Cargill to oppose inclusion of any "upstream subsidies" language in U.S. trade law. That conclusion is based on the implications of an "upstream subsidies" concept for trade policy, its marginal relevance to the problems of the U.S. nitrogen industry and its adverse effects on agricultural and national interests.

TRADE POLICY ISSUES

Maintaining a balanced U.S. trade policy is difficult in today's world. Business cycles put severe strains on all economies and on the political base of support for a progressively more open world trading system. The historical shift from an era of U.S. economic hegemony to a world of increasingly competitive national economies has altered the form of leadership the United States can exercise in liberalizing trade. Various levels and forms of government participation in national economies, in the process of development and in the growth of specific industries have made equity a more pressing and elusive goal in trade policy.

Historically, U.S. trade policy has aimed at progressive liberalization of trade because of the enormous contribution comparative advantage can make to U.S. and world economic growth. The natural corollary to that commitment is restraint on governmental actions that confer an unfair advantage in trade.

U.S. policy, complex in practice, has been relatively straightforward in its conceptual approach to unfairness. It has recognized that all nations, including the United States, have a sovereign right to pursue policies they believe accelerate their development. The line has been drawn, however, where those policies confer benefits on exports not available for domestic industries. So, subsidies are attacked where they aid exports directly or where, though domestic in nature, they benefit exports over local industries in practice.

One segment of U.S. nitrogen producers (but not all, since, for example, Cargill produces nitrogen domestically as do many other firms not supporting the "upstream subsidies"concept) has sought relief from nitrogen imports under established U.S. trade policy. Their case was fully considered and just as fully rejected as recently as four months ago.

In that case, this group of companies argued that the Department of Commerce should find that Mexico's so-calleld two-tier natural gas pricing policy constituted an illegal bounty or grant. In its final negative countervailing duty determination

(June 22, 1983), the Commerce Department concluded clearly and unequivocally "that the pricing differential for export and domestic sales of Mexican natural gas confers neither an export subsidy nor a domestic subsidy upon the Mexican ammonia industry." The Commerce Department also ruled squarely against the petitioners on a second important point. It refused to accept the argument that it should apply an "opportunity cost" (i.e., export price) test for the value of natural gas:". . . there would be no basis in law or fact for the use of an opportunity cost concept. The opportunity cost concept is totally speculative. . . ."

Having failed under existing trade law, some domestic nitrogen producers are seeking to have Congress redraw the line between fair and unfair advantage. They propose a line that goes well beyond the notion of governments providing exporters preferences or goods or services below cost. They seek to label as illegal governmental policies that provide natural resources to national entities at above cost but below prices charged to foreign entities.

We believe this is bad trade policy. It infringes upon national policies that properly are within each country's economic sovereignty. The consequences of such a change are far-reaching and unwise.

What is government's role in ensuring that the playing field is level for all competitors? Preferential treatment for exporters over domestic producers or providing goods or services below cost are covered under existing policy. But the "upstream subsidies" concept invites governmental action to neutralize natural cost advantages. Some of the proposed benchmarks for calculating the "upstream subsidy" illustrate the problem.

One proposed test is the difference between the domestic and world prices of natural gas. If a nitrogen exporting country were to stop selling natural gas into export, would this make the world price irrelevent? Or, would a fall in the world price for gas change the subsidy, even though the government's policy didn't change?

Another proposed benchmark is the difference between the exporter's home market price for gas and the average gas price for U.S. users. But, an average price can hardly be representative when many U.S. nitrogen producers pay two or three times more for gas than the one-third of the industry with the cheapest gas supplies. How can the U.S. insist on an average price benchmark when its own policies produce such disparities?

Another possibility is the opportunity cost for the gas going into the production of nitrogen for export. What is that opportunity cost for a depletable resource that could be left in the ground for future sale at potentially higher prices? Or, what is the opportunity cost for additional gas sales that could depress the world price for all gas, including that country's current exports? Or, what is the opportunity cost for gas that otherwise will be flared off?

In fact, natural resources in a world of sovereign nations have values that are determined by the uses to which those nations can put them. If they can't use them for their own economic development, why should they develop them? The current law protects against direct subsidies or trade discrimination. To go beyond that looks like a trade policy grounded in economic power rather than in considerations of fairness. Moreover, to go beyond that undermines the concept of comparative advantage that underpins the capacity of trade to foster overall economic growth on the basis of free, mutually beneficial commercial exchange. On trade policy grounds alone, therefore, the "upstream subsidies" concept should be rejected.

RELEVANCE TO U.S. NITROGEN INDUSTRY PROBLEMS

Beyond this, however, nitrogen imports that would be shut out by the "upstream subsidies" concept are not really the cause of current depressed prices and closed capacity in the U.S. nitrogen industry. Those problems are endemic to an industry characterized by: large cyclical swings in demand; production capacity that comes on stream only with a long lead time, in large chunks and with a relatively long useful life; and technology and scale-economies generating progressive reductions in production costs. To these factors has been added a shift in relative raw material costs brought on by ending a U.S. policy of under-pricing gas and the opening of new, low-cost fields abroad.

The industry's current problems are particularly acute because a long-term structural adjustment is occurring at the same time as an unanticipated, sharp cyclical drop in product demand. The nitrogen industry enjoyed an unprecedented seller's market in the mid-1970s and a relatively good market at the start of this decade. In response, total U.S. fertilizer consumption rose from 43 million short tons in 1975 to 54 million tons in 1981. Nitrogen use ballooned from 8.6 to 11.9 million short tons in the same period, a 40 percent growth.

Upward trending demand encouraged further plant expansion, but anticipated growth in use has not materialized. The 1980 Soviet grain embargo, a prolonged worldwide recession, falling inflation and rising unemployment, mounting liquidity problems among developing countries and a strong U.S. dollar have combined to drop U.S. grain exports by 15 percent since 1980. Domestic grain use also has stagnated. As surplus grain stocks drove prices down, farmers—caught in a cost-price squeeze—cut back on inputs like fertilizers. This year's payment-in-kind program added to the fertilizer industry's problems by taking 80 million acres out of production. As a result, total U.S. fertilizer use in 1983 is projected to fall below 43 million short tons—less than in 1975. Nitrogen use fell even harder, declining by roughly one-fourth.

Naturally, this resulted in a sharp cutback in U.S. ammonia production—from 19.3 million short tons in 1981 to less than 14 million tons in 1983. Earnings fell and substantial excess capacity emerged. In this respect, the nitrogen industry's problems resemble those elsewhere in agriculture. Farm equipment sales have plummeted. At one point 30,000 covered hopper cars and 3,000 grain barges were idled. U.S. export elevator capacity today is easily 7.5 billion bushels, compared to exports this year of 4.5 billion bushels.

What is surprising is that the U.S. nitrogen trade balance remained relatively stable. In fact, imports gained only about 500,000 tons compared to U.S. nitrogen exports. This is roughly one-tenth of the reduction in U.S. production over the same period.

Clearly, the nitrogen industry's current problems stem overwhelmingly from a cyclical downturn in U.S. agricultural markets after a decade of unparalleled growth. Its current situation would not be materially different if the world nitrogen market were simply subtracted away.

Though cyclical phenomena are the basic cause of the U.S. nitrogen industry's current circumstances, there is more to the story. The world nitrogen industry is being restructured as technological change, scale economies and raw material costs shift comparative advantage.

Cost savings from each of these is large. For example, D. Gale Johnson, a noted agricultural economist, has pointed out that 1974-level technology can produce nitrogen cheaper than 1960-level technology even while paying $1 per mcf more for natural gas.

Scale economies are an important cost factor as well. The Fertilizer Institute's most recent ammonia cost production survey shows that a plant producing 1000 tons per day has a per-ton production cost about half of the per-ton cost for a plant producing less than 600 tons per day ($96.76 per ton vs. $179.55).

Technology and scale economies, in other words, have the capacity to drive an enormous structural change in the world nitrogen industry. That is exactly what is happening. The United States became a marginal net importer of nitrogen again in 1982. Western Europe—for many years the major exporter of nitrogen fertilizer—became an even larger net importer in the same year. Japanese net nitrogen exports have been cut nearly in half since 1978/79, and Korea saw its net nitrogen exports fall 40 percent in the same period.

Remarkably, total world nitrogen exports have remained relatively steady at roughly 12 million tons annually over the past 5 years, even as this structural change has occurred. New, more-efficient nitrogen exporters are by and large displacing traditional exporters rather than squeezing out producers in importing countries. These new exporters, who have built modern, large-scale plants, also are countries with surplus natural gas resources and a desire to add value to their gas exports.

In a market suffering from a cyclical downturn and experiencing a cost-driven restructuring, low-cost producers determine market prices. In fact, the world nitrogen market has been a buyer's market since 1981. As usage declined while new capacity came on stream, prices fell to restore balance by forcing high-cost producers to shut down. Since the most efficient, large-scale U.S. plants have costs roughly half those of smaller plants, there was ample room for prices to fall.

In this environment, nitrogen exporters are price-takers. They are compelled to meet these falling prices or not meet them and surrender markets. The available evidence suggests that is what happened, as total world nitrogen exports did not grow appreciably. Moreover, there is no evidence that exporters enjoyed subsidized natural gas prices. In fact, the Commerce Department found in its anhydrous ammonia investigation that "Pemex's internal costs for natural gas used in ammonia production exceeded the price of natural gas for industrial users in Mexico. . ."

Finally, it should be noted that the protectionism embodied in the "upstream subsidies" concept will not save the older, smaller, less efficient nitrogen plants attract-ed to the Louisiana and Texas Gulf by cheap gas in the 1960's. Their construction shut down an earlier generation of inland plants. In the coming decade, construction or expansion of newer, more efficient plants in high usage area potentially will restructure the domestic industry again. Technological change and scale economies are part of the cause. So too are the disappearance of cheap gas under U.S. decontrol policies and the re-emergence of transportation cost advantages from proximity to users as key domestic market factors.

In other words, the "upstream subsidies" concept neither explains currently depressed nitrogen prices nor corresponds to an unfair practice. It is the wrong response to a situation that will change as demand recovers and the industry's evolution continues.

ADVERSE EFFECTS ON AGRICULTURAL AND NATIONAL INTERESTS

So far, I have argued that the "upstream subsidies" concept for natural resources is bad trade policy and largely irrelevant to the problems of the domestic nitrogen industry. I would like to conclude by suggesting some broader policy considerations for rejecting it.

For one thing, growth of value-added industries in energy-rich countries will increase their reliability as suppliers. As they sink capital into energy processing and link local employment to those activities, the cost to those countries of cutting off energy exports mounts. Those value-added industries in energy-exporting countries represent insurance for the United States against future energy supply disruptions, since an export cut-off would mean shutting down plants and disrupting local economies, not just closing valves.

Second, such industrialization in many cases also represents sound market development for U.S. exports. Forty percent of total U.S. exports now go to developing countries, and these nations are the key growth market for U.S. agricultural sales. Processing raw materials for export is a logical and important tool for energy-rich countries in earning foreign exchange and raising per capita incomes. Such developments will yield important market dividends to export-oriented U.S. industries.

Third, U.S. agriculture has traditionally been the linchpin in domestic political support for more liberal world trade rules. Inserting the "upstream subsidies" proposal into U.S. trade law could seriously erode that support. Other countries could well retaliate against this new, dangerous form of protectionism. Agriculture loses two ways in such a confrontation-directly as the target of retaliation and indirectly as creeping protectionism slows the overall rate of growth in world output and trade.

Finally, the "upstream subsidies" proposals would hurt U.S. agriculture's international competitiveness. Nitrogen trades in a world market, and countervailing duties or import restrictions will raise U.S. farmers' costs relative to their competitors. U.S. farmers understandably will and should oppose such policies, since protectionism simply passes costs onto them.

CONCLUSION

To conclude, Cargill urges this subcommittee to reject the "upstream subsidies" proposals now before it. By departing from the traditional meaning of a subsidy, they invite unwarranted protectionism in the United States and introduce an idea that could also be hurtful to U.S. industries. They are irrelevant to the nitrogen industry's current problems. And, they are bad U.S. policy for the long-run, discouraging desirable changes in developing countries while disadvantaging U.S. agricultural exports.

Thank you.

Chairman GIBBONS. I regret you are under such time pressure. I realize this is a very important matter to Cargill. We may have to call you back some time on very quick notice, and I hope you will be available.

Mr. JOHNSON. Under the circumstances, I probably missed my plane already. So if you would like to ask additional questions, fine.

Chairman GIBBONS. Unfortunately, I am the only one left, and we will go to the other witnesses. I was trying to get you out on time. We will call you if we need you again.

Mr. Wheeler.

STATEMENT OF EDWIN M. WHEELER, COUNSEL, AMERICAN PETROCHEMICAL CONSUMERS

Mr. WHEELER. Good morning, Mr. Chairman. I represent, as counsel, four major importers of nitrogen and have filed a statement with the committee which I understand the chairman has admitted.

Chairman GIBBONS. Yes, sir.

Mr. WHEELER. I would like the record to show that the National Farmers Organization has endorsed that statement as their position.

Chairman GIBBONS. Which one?

Mr. WHEELER. NFO.

Chairman GIBBONS. Oh, that one. All right.

Mr. WHEELER. I will be brief because the hour is late and you have been patient this morning.

Chairman GIBBONS. That is all right. You are the only opposition witnesses this morning, as far as I am concerned. I am sorry the gentleman from Cargill didn't have a lot of time, because I wanted to go over this a lot with him.

Mr. WHEELER. I hate to disagree with the chairman because of his experience in these matters, but it is significant as we begin our discussion in this case that the magnitude of the change we are about to make and what is propelling that change, we are about to embark upon one of the most profound rewritings of the trade law that has ever occurred.

Chairman GIBBONS. That is right.

Mr. WHEELER. Every nation in the world is watching to see what we do. It is being——

Chairman GIBBONS. I am aware of that. I welcome them to emulate it.

Mr. WHEELER. It is being propelled by primarily ammonia producers.

Chairman GIBBONS. Oh, no it is not, either.

Mr. WHEELER. Mr. Chairman, if you would take a look at page 3 of my prepared statement, you can see that that is a tempest in a teapot.

Chairman GIBBONS. That is why I made it clear a while ago that this goes far beyond ammonia, cement, lead, because this has to do with the whole idea of what is the level playing field going to be. What is the level playing field? When are subsidies objectionable to us?

Mr. WHEELER. Mr. Chairman, is the field unlevel?

Chairman GIBBONS. I don't want you to turn this into that kind of hearing. This is not a narrow products hearing.

Mr. WHEELER. Fine.

Chairman GIBBONS. Good.

Mr. WHEELER. We accept that.

Chairman GIBBONS. OK.

Mr. WHEELER. All right. Let's go to the subsidy issue. That seems to be plaguing the chair more than anything else.

Chairman GIBBONS. That is all I am interested in right now.

Mr. WHEELER. The United States, under current law, has more subsidies and more two-tiered pricing than about anybody that could be drug before this committee.

Let's take, for example, the act of Congress in 1978 on establishing natural gas. A third of the U.S. ammonia today is being produced on natural gas prices based below the Mexican price and, Lord knows, below the Canadian price, the Canadians being the single biggest exporter into the United States of fertilizer. There are 10 or 12 levels of pricing under the Natural Gas Act.

Those producers that are hooked on to a given price level of gas far below the so-called $3 figure espoused here this morning are in effect being subsidized by an act of Congress.

Chairman GIBBONS. Are they injuring anybody?

Mr. WHEELER. Certainly, they are, because we are exporters, also.

Chairman GIBBONS. They ought to have a cause of action against them.

Mr. WHEELER. I am not representing the overseas——

Chairman GIBBONS. I don't believe we ought to live by one law and ask everybody else to live by another one.

Mr. WHEELER. That is what is plaguing us.

Chairman GIBBONS. You and I are on the same side on that.

Mr. WHEELER. Take a concrete example of what is on today.

Chairman GIBBONS. I am trying to level the playing field. That is means for everybody to play on.

Mr. WHEELER. Precisely. So we start at the same end of the ball park.

Chairman GIBBONS. OK.

Mr. WHEELER. U.S. oil today is decontrolled by an act of Congress. Therefore, it generally reflects the OPEC pricing. U.S. natural gas under regulation, except for gas extracted below 15,000 feet, is regulated by the U.S. Government. I submit that that is two-tiered pricing.

Second action of the Congress, Congress has decreed that no oil or gas out of the North Slope, the site of the biggest reserves now, can be exported. Only we can have access to that oil and gas.

I submit, Mr. Chairman, that that is a blatant two-tiered pricing situation.

Chairman GIBBONS. But that is stupid, too.

Mr. WHEELER. I couldn't agree with you more. But as the judge said, that is the law. Let's go to another one.

The State of California——

Chairman GIBBONS. You haven't said anything that shook me yet. I agree with you. I don't know what that has to do with what we have here.

Mr. WHEELER. We are as guilty of two-tiered pricing as anyone else.

Chairman GIBBONS. Where are we injuring anybody?

Mr. WHEELER. Because ammonia is moved into the world market, it is a commodity like No. 2 corn, and we are just taking advantage of our own two-tiered pricing as much as any other nation in the world.

Chairman GIBBONS. Is anybody complaining about us injuring them?

Mr. WHEELER. Certainly.

Chairman GIBBONS. Where?

Mr. WHEELER. The European petrochemical, saying we are subsidizing them going into Europe. Let me give you another example. We ship——

Chairman GIBBONS. If we are, we ought to be penalized. I would not—I am not trying to protect us or anybody else. I am just trying to level off the field.

Mr. WHEELER. For the world?

Chairman GIBBONS. For the United States as it interfaces with the rest of the world, yes.

Mr. WHEELER. But, Mr. Chairman, that is not the way the world works. One of the things we—a point we tried to make in this is that the subsidy argument does not wash because every country enjoins certain inherited advantages. Our farmers are the best. Our farmers are subsidized nevertheless by the Congress.

Chairman GIBBONS. Not my farmers.

Mr. WHEELER. Not the orange producers or tomato producers, but certainly the grain farmers are. We are hurting the Mexican farmers by——

Chairman GIBBONS. Who is complaining? No one is complaining.

Mr. WHEELER. Because the Mexican farmers don't complain.

Chairman GIBBONS. Because we are not hurting them. It doesn't hurt the domestic corn or wheat in Mexico.

Mr. WHEELER. But they are tremendous importers, and they are paying a premium for that.

Chairman GIBBONS. We are not worried about people complaining in that respect. We are talking about it going in at too low a price.

Mr. WHEELER. But once you open the door—as the conversation went this morning with the lawyers involved, once you open the subsidy door, there is no way to close it.

Consider, Mr. Chairman, when we talk about subsidy and two-tiered pricing, we are talking about diesel fuel, gasoline, all products pouring into the United States that come from two-tiered pricing.

Chairman GIBBONS. You are using what in college we used to call reductio ad absurdito.

Mr. WHEELER. Why?

Chairman GIBBONS. There are subsidies, sure, all over. What we are worrying about are two types of subsidies, subsidies that injure us——

Mr. WHEELER. Where are we injured?

Chairman GIBBONS. This is——

Mr. WHEELER. Mr. Johnson made the point.

Chairman GIBBONS. A lot of people out there think we are injured. That is a question of fact. If we are not injured, there is no case.

Mr. WHEELER. Exactly. That is why I beg the Chair to look at the data. There is not enough ammonia coming into the United States——

Chairman GIBBONS. This is not an ammonia hearing.

Mr. WHEELER. But that is the injury we are talking about.

Chairman GIBBONS. Somebody else will try that case.

Mr. WHEELER. Where is the injury, though?

Chairman GIBBONS. I am not changing the injury test. I am only changing the subsidy test, Mr. Wheeler.

Mr. WHEELER. You keep asking where is the injury. I submit, where is the injury to the U.S. interests?

Chairman GIBBONS. As I say, this is not an injury hearing. This is a hearing on fixing the value of a subsidy. We can have some injury hearing some time, if that becomes a problem. But now is trying to fix the value of the subsidy.

How do you measure it? How do you measure it, Mr. Wheeler? What is a true, effective measure of it?

Mr. WHEELER. The Chair is saying we are precluded from objecting to going the 4015 route of Henson Moore because we object to the Henson Moore bill in toto.

Chairman GIBBONS. You can talk about anything you want, but all I am interested in is what is the value of the subsidy. I am interested in the propositions we have before us.

Mr. WHEELER. But if the subsidy does no injury, what difference does it make?

Chairman GIBBONS. I agree. What difference does it make?

Mr. WHEELER. Right.

The numbers show there is no injury.

Chairman GIBBONS. I am not arguing that. That is not the question before us. The question before us is what kind of change do we make and how we measure a subsidy. We got three proposals before us.

Mr. WHEELER. Let's talk about that.

Chairman GIBBONS. Three proposals to measure that. All three of the proposals would require a finding that there had to be——

Mr. WHEELER. Material injury.

Chairman GIBBONS. Material injury.

Mr. WHEELER. Right.

Chairman GIBBONS. We don't disagree on injury, fine. If you say there is none, all right; I don't want to argue that. That is another case, another time, another place.

We are trying to define the size and shape and amount of the subsidy. That is the purpose of this hearing today. We are trying to find out how to measure it. We are trying to find out whether or not it is a violation of the GATT.

Mr. Rivers, who by his unique expertise of having served as a trade counsel in the Senate during this time and having served as the negotiator for the United States of America at the negotiations carried on under the Tokyo round on this specific subject, said that it is not a violation of that. I don't know of any living human being in the United States that knows more about this subject and better qualified to talk about it than Mr. Rivers.

Mr. WHEELER. But suppose the nation doesn't belong to GATT and is involved; what is the significance of it?

Chairman GIBBONS. They can join GATT. They have the opportunity to join. If you are telling me that the Mexicans won't join GATT, they have an invitation to join any time they want to.

Mr. WHEELER. Mr. Chairman, I don't speak for the Mexicans.

Chairman GIBBONS. I know. But I just want to make it clear. I have been waiting for somebody to say, oh, the Mexicans are not members of GATT. Well, you know, that is not Sam Gibbons' fault, not the United States of America's fault, not GATT's fault.

Mr. WHEELER. It is not my fault.

Chairman GIBBONS. Good.

Mr. WHEELER. I can see that we are not in agreement on whether or not we ought to look at the injury situation.

Chairman GIBBONS. I just want to focus it. I want to focus on what the hearing is about.

Mr. WHEELER. Let me conclude——

Chairman GIBBONS. I am not interested in wandering all over the globe.

Mr. WHEELER. Let me conclude on raising several issues. We are opposed to the raw material language concept.

Chairman GIBBONS. I understand.

Mr. WHEELER. The question then comes, if you start calculating the value of the duty, which U.S. domestic gas price does the Congress intend for the ITA to follow? Do we take the cheap contract of 25 cents a thousand cubic feet? Do we take the decontrolled gas price of $7? This is a very, very——

Chairman GIBBONS. It is the difference between what they sell it to their own folks for and what they sell it at the border for.

Mr. WHEELER. But they sell it at the border under a solemn agreement with the U.S. Government. And Mr. Johnson is right. If you recollect, Mr. Chairman, during the gasoline shortage our country begged Canada and Mexico to enter into a contract, and they did so, and the price is set at $4.40 by agreement of two administrations.

Chairman GIBBONS. I remember it. I am not—that is not the argument. You want to lead me off to something that is irrelevant and immaterial.

Mr. WHEELER. No, sir.

Chairman GIBBONS. All I am trying to do—you are a good lawyer, Mr. Wheeler, but I made those arguments when my facts weren't very good. So I recognize them.

Now, let's get back to the subject. How should we measure a subsidy? How should we measure a subsidy?

Mr. WHEELER. The tests are before the committee. We can't——

Chairman GIBBONS. You want to stick to the old law.

Mr. WHEELER. Absolutely.

Chairman GIBBONS. OK.

Mr. WHEELER. We just don't think it is warranted in this case.

Now, as to measuring the subsidy, there are diverse and sundry ways to do that. The only thing I should point out is that as U.S. gas prices rise higher and higher and higher, the duty is going to become more and more onerous. Somewhere the U.S. price has to figure in there on the, quote, "fair market value," unquote.

Now, I assume from hearing Mr. Moore before the committee this morning in the discussions today he wants that $4.40 price included in part and parcel of his diverse tests, but we are in a quandry to know what this duty will really be other than on ammonia it will be $85 a ton, if you put all the so-called tests together.

We simply take the position—and I conclude on it—that there is no reason to go into this morass; that injury to U.S. industry has not been shown.

Thank you.
[The prepared statement follows:]

STATEMENT OF EDWIN M. WHEELER, COUNSEL, AMERICAN PETROCHEMICAL CONSUMERS

Mr. Chairman, Members of the Committee and Staff:

We appreciate the opportunity to appear before you today to testify wherein the Chairman has directed that we limit our testimony to only one aspect of the proposed "Trade Remedies Reform Act of 1983."

Several days ago, we distributed to every member of the Committee a detailed paper with comments and supporting data which contains our objections to several sections of the proposed legislation including the issue we are limited to here today.

The American Petrochemical Consumers Group that I represent as counsel are all major importers of nitrogenous fertilizers. One member has a contract for long term purchases based on an exchange for U.S. fertilizers and the others buy essentially on a year-to-year basis. They are unalterably opposed to imposition of duties based on raw material costs differentials. By way of self-introduction, I have had nearly fifteen years of experience as president of The Fertilizer Institute which is the national trade association of the U.S. industry. I left that position in January 1983, and am a sole practitioner here in Washington, D.C. with offices at 1815 H Street, N.W., Suite 1000.

We believe the proponents of placing a duty on a nation whose government establishes prices on raw materials going into a manufactured product have no case. It is true that twice the Ad Hoc Ammonia Producers have lost before the International Trade Commission, but in neither case did they demonstrate any need for so drastic a change in the law as they now propose.

What the ammonia producers are complaining about is that they are unable to buy the biggest component that goes into making ammonia (82% nitrogen) at the same price as certain non-U.S. producers. What they fail to tell you is that within this group there are those who have long term contracts for very cheap gas themselves. Fully one-third of U.S. production of this commodity is produced using gas that costs $1.00 per mcf or less. On the other hand, average U.S. well head prices are are in the $2.75 - $3.00 range. Do not be misled, for the Ad Hoc Ammonia group does not represent all of the U.S. nitrogen producers and certainly does not represent importers, wholesalers, retail dealers or farmers.

The proponents seek <u>only</u> higher nitrogen prices by excluding certain competitors. Higher fertilizer prices will be a blow to U.S. farmers whose cries of anguish are familiar to this committee via all of the news media. Higher fertilizer prices mean higher food prices because nitrogen fertilizer is heavily used on every major crop except soybeans. Commercial fertilizers enhance our farmers' output by more than 30%.

In the fertilizer year (7/1/82 - 6/30/83) just ended we produced, imported and exported the following quantities of nitrogenous fertilizers:

Product	U.S. Mfg.	U.S. Exports	U.S.# Imports
Ammonia	13,039,834	425,900	2,144,076
Urea (Liquid & Solid)	9,069,096	1,317,000	1,705,925
Ammonium Nitrate (Liq. & Sld.)	8,734,372	30,100	333,624
Ammonium Sulphate*	1,777,829	660,100	383,996
Nitrogen Solutions	6,597,575	121,300	129,217
Total	39,218,705	2,554,400	4,696,838

#Sources of imports shown on attached exhibit.
*Mostly by product from other petrochemical production or steel manufacturing.

One can see that we as a nation are a long way from being dependent upon foreign sources of nitrogen. Much of our domestic and imported ammonia is combined into other fertilizer products that also are exported, which is not reflected in the above data. Nearly two million additional tons of ammonia, not shown on the preceding data, are exported in phosphatic materials, primarily through the port of Tampa, Florida. U.S. exports of all fertilizers (including phosphate rock) are in the 18+ million ton range. Because we too, price natural gas on a two-tier system, 6 or 7 million tons of these exports would be subject to recrimination. It should be noted that by all odds Canada is the single biggest supplier of our imports of nitrogen - not Mexico, not the Soviet Union.

The parodox of the Ad Hoc Ammonia group's position is that they are not only advocating higher U.S. domestic fertilizer prices, but that they seek to place a heavy penalty on those same nations which are large purchasers of U.S. farmers' grain. Truly, they are penalizing our farmers coming and going! This subject will be discussed in full by other witnesses here today.

Mexico prices its natural gas to all industries in that country at the same price. The petrochemical industry in that nation is on the same basis as any other. The gas they export to the U.S. is done so pursuant to an agreement between our government and their government. We find this same general situation obtains in Canada albiet the provinces (primarily gas rich Alberta) set the local price. Both the Carter and the Reagan Administrations have entered into these agreements, modifying the price downward some few months ago. Thus, the two-tier situation is established or blessed by the governments of the nations involved.

Mexico supplies the U.S. about 800,000 barrels of crude oil a day, out of the 1,500,000 it produces. With the oil comes gas which they can either burn (flare) or use in Mexico. Should we penalize the leading supplier of U.S. crude oil by this tariff? Should we compel flaring? What a waste. What a slap in the face to the nation that buys tremendous quantities of U.S. manufactured goods and farm products.

We fail to see the two-tier argument in either of these nations because you can not lawfully take gas from Mexico or Canada except under the terms of the governmental agreement. We do not deny that Mexico will not permit U.S. producers to locate ammonia plants in Mexico. Canada does and C.F. Industries, J.R. Simplot and Exxon's subsidiary, Esso, have major installations there. Congressman Moore's proposal would penalize these plants as any other, regardless of where they are located.

California's legislature and Oklahoma's Public Service Commission have given specific lower gas rates to the ammonia producers than to any other user of gas within their state. Two-tier? Yes, sir! We do not permit the export of Alaskan crude oil or gas. Two-tier? Yes, sir!

Proponents argue accessability viz., if we can buy gas at the same prices as the local competitor, then we ask for no duty. They know full well and we hope the Committee fully understands that, by the very nature of Communism we will <u>never</u> be able to get gas from Russia or locate U.S. owned plants there, which means there will always be a duty. Yet, they failed to prove Russia was dumping in the Ad Hoc Ammonia Producers v. Oxy case.

Nor were they able to show that Mexico was a price cutter of ammonia in the last case they lost. Neither of these sources are price cutters because they must earn maximum U.S. dollars to pay for their imports of American farmers' grain or U.S. fertilizers.

America's import policy going back over decades has always been to favor those nations having a natural or inherent advantage of raw materials, cheaper labor, proximity to market, etc. The proposal before the Committee is a complete departure from a wise and proven course. To sail now upon a 180° change will put us on the shoals of recrimination at a time when a change in azimuth is not even indicated.

Looking down the road this legislation, if enacted, would pit the natural gas residental consumers in a bidding war against the U.S. petrochemical producers for our diminishing supply of gas. Why we, as national policy, would want to disrupt the flow of gas (in the form of petrochemicals) at reasonable prices absolutely escapes us. Surely this Congress does not want to say to the homeowner "I have raised your gas prices to help a multi-billion dollar group of manufacturers."

Thus, we array ourselves on the side of open trade, the side of the consumer, the American farmer-exporter.

No matter which of the various tests the Committee selects as to "fair market value" we will protest the basic concept to the end. Using just the simple example of gas in Mexico at S.50

per mcf and U.S. average cost of $3.00 means a countervailing duty of $87.50 per ton of ammonia which sells currently at $145 per ton. Whether you delineate the "fair market" price by any description or title, the duty is totally out of proportion to the selling price and will stop all imports. "Fair market price" is not fair to farmers or consumers.

Current law has withstood the tests of a tremendous growth in world commerce. It is not perfect, as we all recognize. Nevertheless, "improvement", disguised by any strategem which builds a wall around the United States and which will bring swift retaliation should not be approved by the Subcommittee on Trade.

Respectfully submitted,

Edwin M. Wheeler
Counsel
American Petrochemical Consumer
Suite 1000
1815 H Street, N.W.
Washington, D.C. 20006
(202) 466-4583

ATTACHMENT 1

U.S. Nitrogen Fertilizer Production
and
Imports in Tons
(July 1, 1982 - June 30, 1983)

Product	U.S. Production		Imported
AMMONIA	13,039,834		2,144,076
Source of Import			
Canada		635,235	
Mexico		531,488	
U.S.S.R.		473,145	
Trinidad-Tobago		377,237	
Venezuela		49,154	
French West Indies		48,159	
Netherland Antilles		23,786	
Colombia		5,779	
UREA	9,069,095		1,705,925
Source of Import			
Canada		720,219	
Norway		3,103	
United Kingdom		9,681	
Netherlands		347,656	
Federal Republic of Germany		14,258	
Mexico		1,206	
Trinidad-Tobago		14,400	
Ireland		8,482	
U.S.S.R.		261,135	
Venezuela		122,243	
Qatar		69,374	
Brazil		34,588	
French West Indies		14,397	
New Zealand		9,612	
Romania		74,828	
Japan		737	
AMMONIUM NITRATE	8,734,372		333,624
Source of Import			
Canada		213,239	
Netherlands		120,385	

ATTACHMENT 1 (Continued)

Product	U.S. Production		Imported
AMMONIUM SULFATE*	1,777,829		383,996
Source of Import			
Canada		229,032	
Federal Republic of Germany		24,908	
Netherlands		71,676	
Belgium & Luxembourg		12,673	
Norway		19,571	
Japan		12,118	
Trinidad-Tobago		14,018	
*May include by product from steel manufacturing, etc.			
NITROGEN SOLUTIONS	6,597,575		129,217
Source of Import			
Canada		97,992	
Norway		25,878	
Netherlands		5,347	
TOTAL U.S. PRODUCTION	39,218,705		
TOTAL IMPORTS			4,696,838

Chairman GIBBONS. If there is no injury to U.S. industry, what change we make doesn't make any difference, anyway. That is my final observation, Mr. Wheeler.

The National Grange is next.

STATEMENT OF ROBERT N. HAMPTON, ON BEHALF OF EDWARD ANDERSON, MASTER, THE NATIONAL GRANGE, AND ON BEHALF OF THE NATIONAL ASSOCIATION OF WHEAT GROWERS, ACCOMPANIED BY JOHN B. REHM, PARTNER, BUSBY REHM & LEONARD

Mr. HAMPTON. Thank you, Mr. Chairman.

I am appearing for Mr. Anderson, who is the Master of the National Grange, and he expressed his apology that, being out of town, he was not able to get back.

Chairman GIBBONS. All right, sir.

Mr. HAMPTON. Mr. Chairman, I would like to submit my entire statement and make a few comments on the highlights of the statement.

Chairman GIBBONS. Go right ahead.

Mr. HAMPTON. I think you stated succinctly and appropriately in one of your earlier statements the fact that one of the most sweeping—and, I would say, the most insidious threat to more open and expanded world trade—is this matter of subsidies. It was the knotty issue during the Tokyo round, and we have had a terrible time trying to get a handle on an international code of rules to deal with export subsidy abuses.

Chairman GIBBONS. Yes, sir.

Mr. HAMPTON. There has been a great deal of debate as to whether we made any progress in the Subsidies Code. One would have to concede that little more than an embryonic effort came out of the Tokyo round. You are aware that no one understands better than U.S. agriculture the threats and the dangers and the costs that we suffer from unfair subsidies which we have not been able to deal with through the existing section 301 provisions that we have tried to use in connection with the increasing use of subsidies by the Europeans in recent years.

Now, the indirect subsidies that I think you are really tackling here are very difficult to define and to measure, and that seems to be the central issue. I don't think there is any difference of opinion among us about the importance of our trying to reduce the bad effects of these subsidies on American interests and on world trade.

So the discussion here today should focus on this central question: How do we find a way to deal with subsidy abuses appropriately, so that we don't create bigger problems than we solve? I am sure that we are together on that objective.

There are two things that are central to the concerns of the National Grange, and I can speak also for the National Association of Wheat Growers, who will submit a further statement on their concern about two matters. First, it appears quite certain that action of this kind would threaten very seriously to raise the cost of hydrogen fertilizers to U.S. farmers. Farmers are having enough difficulties with costs today and that would create great additional problems for them. It could also create even greater problems indirectly by damaging farmers export opportunities as a result of any unwise unilateral actions which would invite retaliation by our major international trading partners.

I might refer specifically to the Chinese situation where the Chinese did cut back severely for a time on our export opportunities because we made a rather abrupt, and in the textile case an unwise decision to restrict their imports. We know that type of unilateral action is dangerous and counterproductive. The gist of our argument is that proposal for such actions are so serious that we should consider them much more carefully and fully than the current timetable seems to permit.

We have appealed to you in a letter of October 13, 1983 along with eight other agricultural organizations, that we would like this proposal to be approached in a more deliberate fashion. We have asked that other elements of this bill which we believe are even more sweeping, but raise similar questions, should also have hearings by your subcommittee—and that is our major request today. We are so concerned about additional costs and the threat to our potential export markets that we would like to suggest that further study by an appropriate agency, commission, or congressional group be made, and that we not act too abruptly or without due consideration to try to correct this serious subsidy problem which is always with us and which is getting to be, as you said, increasingly important in all our trade interests.

[The letter referred to follows:]

NATIONAL ASSOCIATION OF WHEAT GROWERS,
Washington, D.C., October 13, 1983.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C.

DEAR CHAIRMAN GIBBONS: Representing the trade interests of American farmers and agricultural exporters, we are seriously concerned with the potential threats to our export markets from the export targeting subsidy and other sections of the "trade remedies reform" draft bill.

The dangers of retaliation and critical disruption of the world trading system from such a unilateral and ambiguous broadening of the countervailing duty authority deserve careful and thorough evaluation. We strongly urge that you expand the scope of your hearings to include, in particular, those portions of the bill dealing with export targeting subsidies. This is a matter of vital importance for U.S. agriculture.

Sincerely yours,

American Soybean Association, National Association of Wheat Growers, National Broiler Council, National Corn Growers Association, National Grain Trade Council, National Grange, National Soybean Processors Association, Millers National Federation, and Rice Millers Association.

Mr. HAMPTON. We thank you very much for the opportunity to appear before you today.

[The prepared statement of Mr. Andersen follows:]

STATEMENT OF EDWARD ANDERSEN, MASTER, THE NATIONAL GRANGE

Mr. Chairman and Members of the Subcommittee: Since its beginning in 1867, the National Grange and its 425,000 farmer and rural members throughout the U.S. have always considered trade issues to be crucial to the health of our rural, national and world economies. At no time in our history has that been more true than in our modern, increasingly interdependent world. Farmers, industrialists, retailers, workers, consumers—we are all dependent every day not only on how our own government deals with fiscal and monetary issues and other trade-related policies, but on how it deals with comparable policies of our trading partners throughout the world.

We appreciate the efforts of this subcommittee to deal with a host of today's trade-related problems growing out of increasing productive efficiency in other countries or of unfair barriers or distortions to trade which pose critical problems for many sectors of the American economy. Loss of export markets, unemployment, business failures and unnecessarily high costs to American consumers are among the most serious of such problems.

As you know, American farmers are facing serious difficulties for many reasons today—high interest and operating costs, drought, and in many important export markets, unfair subsidies or other trading barriers or practices which have blocked us from markets which we should have. Following the sensational export market growth in agricultural exports during the 1970's from less than a $10 billion level in 1972 to more than $40 billion annually, we have experienced serious losses in the past two years, declining from the 1981 peak of almost $44 billion to less than $35 billion forecast for 1983. These losses are due in large measure to unfavorable exchange rates, in some cases declining purchasing power of our foreign customers, and to unfair export subsidies by European, Brazilian and other agricultural exporters.

Consequently, we have consistently urged U.S. trade leaders to deal with these serious trade problems, if possible through major multinational efforts such as those of the Tokyo Round and earlier major trade negotiations, and through corrective actions taken within the framework of the General Agreement on Tariffs and Trade which provides the trading rules on which any complex worldwide trading system is dependent.

Our own national measures to assure fairness to American traders within this GATT trading system—laws such as the countervailing duty or anti-dumping authorities and the escape clause and other safeguard provisions are vitally important to U.S. agriculture as well as other trading interests. Countervailing duty authority is among the most important of such measures.

We are concerned about trading practices from suppliers abroad which require us to countervail and we share the concerns of American industry "upstream" and other targeting subsidies.

However, the natural resource proposal raises some serious questions. First, countervailing against low-priced foreign componenets of a natural resource such as Mexican natural gas, for example, would inevitably raise costs of nitrogenous fertilizers to U.S. farmers. In the present seriously depressed agricultural economy, our farmers can ill afford additional unnecessary costs for inputs which they must have to produce food and fiber efficiently.

Another serious consideration is the question of the reaction of some of our major foreign customer markets for grain and other U.S. farm products, such as Mexico and Russia. We have recently seen the Chinese reaction to a similar U.S. action in textile imports, and we know from painful experience with grain embargoes against the U.S.S.R. how badly our export markets have suffered from sudden, unwise or arbitrary U.S. efforts to restrict trade, or raise other questions as to supply reliability. We fear that such unilateral efforts to redefine criteria for countervailing duties would indeed risk serious threats to important U.S. agricultural exports, not only as a direct retaliation but in the longer term because it appears to violate the principle—which is in both the GATT subsidies code and our existing domestic law—that governmental assistance is not countervailable if such assistance is available to all industries within the country.

This proposal is of such broad potential consequence that we believe it deserves much more comprehensive study by an impartial commission or agency to weight these serious questions against any potential national benefits. The National Grange has expressed its concerns, along with eight other agricultural organizations in a request to this subcommittee that these hearings be broadened to include other and even more sweeping elements of the Trade Remedies Reform Act of 1983. While we appreciate the desire for early action on important and difficult subsidy issues, more deliberate consideration of these extremely complex issues is needed or order to insure that any proposed changes in our law are clearly in the national interest, and fully consistent with our international commitments and obligations.

We appreciate the opportunity to present our views before this committee.

Chairman GIBBONS. I appreciate your concern. I think we moved with anything other than deliberate speed. We have been working on this for years off and on. We have had tons of hearings on the matter at one time or another. We welcome anyone's views on it. We invited anyone with views on it to write us a memorandum or a letter which we could examine and see whether or not it was germane, and that is one of the reasons we are having this hearing today.

As I say, I regret that the Cargill Corp., which is an important worldwide business and has a lot of experience in this, was under such time constraints today. I think it would have been appropriate to go into a lot of things and have all the members of the committee have a bit of time to talk to Cargill, and to talk to the rest of you, too. But we can't sit around and sit around forever.

Mr. REHM. Mr. Chairman, could I make a few points?

Chairman GIBBONS. Sure.

Mr. REHM. I want to get to what you, I think, properly identify as the heart of the matter: Do we have a subsidy here? I guess anybody can define subsidy as he wishes. I think the question should be refined to be: Do we have an actionable subsidy here; that is to say, do we have a subsidy against which countervailing duties would be appropriate?

You have said several times this morning that you want to level the playing field. In our judgment, the proposal would destroy the playing field. I say that, and I am using that word very seriously, Mr. Chairman——

Chairman GIBBONS. I understand.

Mr. REHM [continuing]. Because I think that inevitably and inescapably the proposal must depart from and overthrow the principle of general availability. That principle, it seems to me, makes eminent sense. It makes eminent sense—though I am not an economist—because as the Department of Commerce told you earlier this morning, and I quote from Mr. Holmer's statement, generally available domestic subsidies do not distort the allocation of resources within an economy.

I don't belabor that because I don't pretend to be an economist. I am a lawyer.

Let me turn to the violation of the Subsidies Code. We have received already I think two different opinions, one from the present General Counsel of the USTR, and another from a previous General Counsel. Since I was the first General Counsel of STR, I will throw in my opinion for what it is worth.

I think we do have a violation of the GATT Subsidies Code here, and I will tell you why as explicitly as I can so at least you will understand me, though you may disagree.

Chairman GIBBONS. All right.

Mr. REHM. First, and in this respect, I fully agree with Claud Gingrich. He chose his words carefully, for obvious reasons. He was speaking for the administration, and the administration doesn't want to easily acknowledge a violation, particularly if the provision should be enacted into law. That would be disadvantageous legislative history.

Chairman GIBBONS. I recognize that.

Mr. REHM. But he did say very clearly, relying on article 1 of the Subsidies Code, which says in effect—I don't have it before me—that the signatories to the code are permitted to impose countervailing duties only in situations described in the code. And he said that if countervailing duties were to be imposed under this new amendment, because the code doesn't provide for this kind of upstream subsidy, the action of imposing the countervailing duties would not be authorized by—his language was, would not be in conformity with—the code. In my view, that is tantamount to acknowledging a violation.

I have a second reason, however, for suggesting there would be a violation. Paragraph 3 of article 11 of the code, in dealing generally with the concept of domestic subsidies, clearly establishes on its face—and I can read it to you if you wish——

Chairman GIBBONS. Would you, please?

Mr. REHM. Yes, indeed.

I might for your benefit, Mr. Chairman, say that article 11 is entitled "Subsidies Other Than Export Subsidies."

Paragraph 3 reads:

> Signatories recognize that the objectives mentioned in paragraph 1 above may be achieved, inter alia, by means of subsidies granted with the aim of giving an advantage to certain enterprises.

And then examples of possible forms of such subsidies are given, and there is a list there which I don't need to read.

I am not pretending, Mr. Chairman, that this clearly resolves the question. You know as well as anyone in this room that the Subsidies Code was the product of endless negotiations, compromises and the like.

All I am saying is I think one can find in the code itself, by express language—this is why I call this my second argument—the fundamental notion of the principle of general availability.

Let me move on beyond the question of the violation of the GATT Subsidies Code, about which people can obviously disagree.

My deepest concern and I think one of the deepest concerns of all the gentleman you have heard from in this panel is where are we if we eliminate the principle of general availability? My deepest concern is, and I guess I am one of the few like yourself, free traders, left, where do we stop the process of imposing countervailing duties?

It seems to me that once you abandon the principle of general availability—and I don't think I am being melodramatic or ridiculous in suggesting this—one country can judge another country's corporate income tax structure. As we all know, European countries have significantly higher corporate tax rates than this country. Is this a subsidy the U.S. Government provides to U.S. corporations?

I would say on its face, absolutely. What about investment tax credits made available to industries in this country which are greater than those of other countries? It seems to me inescapable that, if you depart from general availability and don't focus on special Government measures provided to specific industries and enterprises, investment tax credits are fair game.

Accelerated depreciation schedules, reconstruction finance—the list is endless, as Mr. Frenzel suggested earlier.

Chairman GIBBONS. I realize that.

Mr. REHM. That is why for me this is so important. You are absolutely right, Mr. Chairman, that this has little to do with ammonia or nitrogen or cement or the like. It is a most profound issue that I sense you are most sincerely trying to wrestle with. But our concern is that trying to meet the two-tiered problem which you see as a problem—I may not, but let's assume it is a problem for the purposes of this discussion—our deepest concern is that you are inescapably abandoning such a fundamental concept which now at least creates some structure, some parameters for the manner in which this country and other countries deal with countervailing duties. To abandon that principle is to invite an anarchy. Then any government can of course find any number of measures maintained by another government as constituting a countervailing subsidy.

The injury test is there admittedly, and I agree it is a safeguard to a degree, but do we want to invite that kind of massive use of the countervailing duty statute? That is our deepest concern. To try to cure a problem, assuming it exists, we think you are literally opening Pandora's box and we see no end if we depart from the principle of general availability.

Chairman GIBBONS. Well, you have made a very learned statement there. There are some things I disagree with you on and that is our tax system. But most of the people who come in here when I am wearing my taxwriting hat, say we are discriminating against them severely because our tax system is not competitive. But you realize that that is always argumentative.

But what we are talking about here is, if there is a subsidy, it has to constitute a significant portion of the resulting product's manufacturing cost.

Mr. REHM. You and I are——

Chairman GIBBONS. It has to constitute a significant portion of the resulting product's manufacturing cost.

Now, we could argue about what is significant.

Mr. REHM. To be sure.

Chairman GIBBONS. Perhaps we ought to focus more on that word. But it wouldn't be such things as better roads or better bridges or smoother water or a better railroad or something like that.

Mr. REHM. Why not, Mr. Chairman?

Chairman GIBBONS. Because I don't think anybody could prove that that is a significant portion of the cost of the resulting product.

Mr. REHM. For certain products—and I can't name them——

Chairman GIBBONS. I can't name them either. I don't think anybody can but go ahead.

Mr. REHM. I was just going to suggest, I don't know of a concrete example, but I think we could find one where an important commodity or heavy commodity moves by water transportation and one could establish that a canal perhaps that provides water transportation was built with heavy government subsidies. One might well be able to find that they had a significant impact upon the cost of the completed product.

But, Mr. Chairman, again, our point is—and I recognize and commend you for the fact you are trying to find ways to contain the operation of this program through a variety of means that you have discussed this morning—but I have to come back to your major premise. You are prepared apparently to abandon the principle of general availability, and we would ask you most sincerely to consider what we see as the dire consequences of abandoning that principle.

Chairman GIBBONS. Looking at the present and going down to the future—we have got two big problems that America has to face as far as leveling the playing field. The first one is how do we attack nonmarket pricing under our dumping and countervailing duty laws? That is proving to be such a knotty problem that we almost decided to put that one on the back burner. But I am not sure that we ought to at this time. Frankly, it is my current intention to go back to that nonmarket pricing matter again, because everybody realizes that we have not found a workable solution for the nonmarket economies.

Mr. REHM. We would agree.

Chairman GIBBONS. The second thing is that subsidies are a growing practice throughout the world. As I travel around the world—and I travel a lot and I listen a lot and I look around a lot—the subsidies thing is going to overwhelm us if we don't put an end to it.

GATT, because of its structural problems, cannot lead. It must go along. America has to lead. If we don't lead no one else is going to lead. If we don't begin to grab hold of the subsidies problem and do something meaningful about it our economy is going to be so distorted. We have got people running for President who say we ought to get into the subsidies battle and start outsubsidizing everybody else. In fact this Government already started outsubsidizing everybody else on wheat. Lord knows where this crazy thing will end unless we do something constructive about it.

What I am proposing here and what the committee is proposing is not the final answer. There never will be a final answer in this area. Once we do something then everybody says, well, we can get around that by so and so. Well, maybe they can. There is no final answer. We just have to be alert and try to anticipate these things and plug them up as we get to them, but try to have the overall objective that we will keep the international field level.

We don't care what happens as long as it doesn't injure us. They can do any crazy thing they want to in the nonmarket economies or in the highly subsidized economies. I don't want to interfere in their own affairs. But when it does cross the borders and starts to injure us, then it is a matter of concern. None of this that we are doing means anything if it doesn't injure us.

Mr. REHM. Do you share our concern, Mr. Chairman, about abandoning the principle of general availability? About opening up a Pandora's box?

Chairman GIBBONS. That is the argument that everybody makes anytime you try to make the law, opening up Pandora's box.

Mr. REHM. It seems to me in this case——

Chairman GIBBONS. I am concerned about it but I am more concerned about the growing of a real thing that I see out there in the international community and that is the growth of additional subsidies. Not only are other countries doing it but we are at the same time tempted to do it because no one will put a halt to it. That is our problem. Somebody has to say "halt."

Then we will all begin to do something about it and do something constructive about it. But the way we are going now it is like the guys at a beer party and the beer hasn't run out, everybody is going to have one more. That is the problem we are in. Unless we say, you know, "The beer's all gone, go on home," this party will get wilder and wilder. That is what we are up against as legislators here.

Mr. REHM. Whether we like it or not, since as you well know, we operate within an increasingly and highly interdependent economic system throughout the world, it seems to me we have to pay attention to the rules of the game and what the rules of the game should be.

Chairman GIBBONS. I don't want to violate the rules of the game.

Mr. REHM. It seems to me once you depart from the principle of general availability, perforce you have no rules anymore, then anything is literally a subsidy, and all of the painstaking efforts to begin to define an export subsidy, a domestic subsidy, and, within the ambit of domestic subsidies, an upstream subsidy, all that goes by the boards. Then everyone can do what he wants. Then it is anarchy.

It seems to me that that is the necessary consequence of your proposal, although I know you are struggling mightily to deal with a narrower issue. The door would be flung open wide. That is our deepest concern.

Chairman GIBBONS. You are saying we have the general availability test in our statute because it is required to be there by the GATT?

Mr. REHM. I don't think I could fairly use the word "require." But I believe that there is a consensus among those who negotiated the code that countervailable subsidies, that is, domestic but not export subsidies would be those made available to specific enterprises. Yes, I believe that is a fair statement, but more importantly——

Chairman GIBBONS. You and Mr. Rivers, who negotiated the agreement, are at opposite ends of the horn.

Mr. REHM. That is correct.

Chairman GIBBONS. You mean the fellow that negotiated didn't know what he was doing?

Mr. REHM. I will not discuss his position or why he is here today. I think it speaks for itself, frankly.

Chairman GIBBONS. Well, if you——

Mr. REHM. That is an aside. Let's assume no violation of GATT for the moment. I come back to my basic problem, which is can we afford to depart from this critical principle? What have we got left in terms of a rational definition of "subsidies" if we depart from and overthrow the notion of general availability? Where are we in the world of domestic subsidies? Literally any governmental measure found to have some significant impact on exports is countervailable.

Chairman GIBBONS. You think we have to accept everybody's two-tiered pricing system?

Mr. REHM. I return to the comments of the gentleman from Cargill. I was in the ammonia case, opposing Mr. Rivers and others, and if, as I believe was true in that case, the government-regulated price was above the cost of production and assured Pemex a profit, although it is difficult to determine because it was an intracompany transfer—assuming those facts for the moment, I don't see a subsidy there.

Admittedly the producer cannot derive as large a profit as he might without the government-regulated price, but, nevertheless, he is recovering his costs and making a profit. And he is taking advantage of a very available, cheap, natural resource. I don't know why that should be called a subsidy. Why should the less competitive U.S. producer require the more competitive Mexican producer to make available the natural gas at that low price? Should any sovereign government be put into that position of giving away, if you will, its comparative advantage? We would be shocked at the idea.

Chairman GIBBONS. They are not compelled to do anything. They don't have to sell anything.

Mr. REHM. That is right. They are free to maintain a lower price within their own economy for their own economic development. As long as that regulated price is made available to all industries, as was clearly the case in the ammonia case, it seems to me that that is a legitimate policy for a foreign government.

Chairman GIBBONS. Then it comes into our stream of commerce and—no, they could——

Mr. SHUSTER. There is no subsidy.

Chairman GIBBONS. They could give everybody 20 tons of ammonia down there and let them do whatever they want with it in Mexico but when they bring it into the United States and injure us, it becomes a problem.

Mr. REHM. The fact that——

Chairman GIBBONS. Whatever the Mexicans do is their own business.

Mr. REHM. You will be the first to agree that merely because injury takes place, it doesn't make it an unfair trade practice. That is clear, is it not?

Chairman GIBBONS. It becomes cognizable then.

Mr. REHM. I hope not. I would hope the question as to whether there is an unfair trade practice would analytically be totally disassociated from the issue of injury. Many industries are being injured in this country and for good reasons. They are not competitive, they are not modernized, not doing what they should to be competitive. So injury for me doesn't even make out a prima facie case of an unfair trade practice. That is a totally separate analytical issue.

Chairman GIBBONS. Well, I will try and analyze that a little more.

Mr. REHM. Again, Mr. Chairman, you have been very, very patient with us, and we thank you very much for listening to us.

Chairman GIBBONS. Anybody else got a statement?

Mr. WHEELER. Thank you, Mr. Chairman.

Chairman GIBBONS. Thank you.

This concludes the hearing for today.

[Whereupon, at 1:10 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

STATEMENT OF KAISER ALUMINUM & CHEMICAL CORP.

Kaiser Aluminum & Chemical Corporation (Kaiser) is vitally concerned and involved with international trade. Five of its seven major operating divisions participate heavily in international activities, including both imports and exports of natural resources and manufactured products.

As a fully-integrated aluminum producer in the U.S. and a participant in all major world aluminum markets, Kaiser is involved in the mining of bauxite, the major aluminum-bearing ore; the refining of alumina, the intermediate material; the production of primary aluminum; and the fabrication and sale of aluminum products to other fabricators and to end-users.

While aluminum represents its largest single activity, a sizeable portion of Kaiser's sales and earnings is provided by its diversified businesses. These include agricultural chemicals, industrial chemicals, refractories and international commodities trading.

In 1982 Kaiser had sales of $2.9 billion and assets of $3.6 billion. It operates 72 major manufacturing facilities in 30 states. Internationally, the company owns or has an interest in facilities in 10 countries.

On October 12—just eight days ago—the subcommittee on trade released a draft bill (dated October 5, 1983) which embodies in legislative language some of the trade law reform proposals it has under consideration. Within the very limited time allowed, we have attempted to review this draft language. The one inescapable conclusion reached is that the technical and complex issues involved demand further time and attention than they have received to date. To the best of our knowledge, this hearing (October 20) is the first opportunity afforded by the subcommittee for interested parties to comment on specific subcommittee legislative proposals. But this has been limited to the narrow issue of whether, and to what extent, two-tier pricing schemes established by foreign governments on natural resources should be treated as subsidies under U.S. countervailing duty law. Even in this limited context, legislative language for the three alternative measurements advanced by the subcommittee for measuring the level of such "upstream" subsidies is not provided.

The other portions of the subcommittee's draft measure, released only eight days ago, are not on the agenda for this hearing. It is our further understanding a formal bill may be introduced and acted upon by the subcommittee within the next few days.

Kaiser believes the comprehensive trade law reform proposals being considered by the subcommittee are very important. However, we are concerned that the subcommittee is attempting to work too fast. The numerous issues involved are extremely complex and, in many cases, the best course of action for the United States is not immediately apparent. From our preliminary review of the subcommittee's draft bill and other legislative proposals (e.g. H.R. 3801 and H.R. 4015), a number of serious questions arise which, in our estimation, require a great deal of further study. The remainder of this statement outlines some of the questions which cause us real concern.

THE ISSUES UNDER CONSIDERATION HAVE FAR-REACHING IMPLICATIONS

Within the last decade international trade has reached proportions well beyond the expectations of many forecasters. The implications are staggering. Many countries in the free world are now very dependent on worldwide trade to support their economies and to service their foreign financial obligations. There have been major shifts in the geographical locations for natural resource development, manufacturing and agricultural products. While this present day interdependence has benefitted some countries, including the United States, it has also caused problems as major shifts and dislocations continue to occur.

The most dramatic shift of all came in the world oil price shocks of 1973 and 1979. These changes were destined to cause a reordering for years to come among those countries with energy resources surplus to their needs and those countries which must import energy or energy byproducts in order to balance their energy requirements.

Only now are some of the full realizations of these energy shocks developing in the United States. As U.S. natural gas and electricity costs continue to spiral upward, and other countries take advantage of their resource positions, the competitive balance changes for many U.S. industries. Investment patterns have already changed with many U.S. companies holding substantial investments offshore in order to continue to offer the American consumer competitively-priced products.

Unfortunately, the U.S. is in a deficit energy resource position and will be for several more decades. This means it must rely on trade to satisfy its energy requirements. The key question is what U.S. trade policies can best serve the economic interests of its citizens. Is it better to import raw energy and retain the necessary manufacturing and jobs in this country, or is it more advantageous to import certain high energy content commodities from areas of cheap and abundant energy; thereby reducing costs to the U.S. consumer and not taxing scarce U.S. energy resources?

These are extremely complex questions. Kaiser believes it is urgent that Congress deal with them; but at the same time they need to be fully explored before legislation is considered. We believe it would be helpful to schedule a series of hearings on the subject. This would afford U.S. companies and others the necessary time to carefully assess whether, and to what extent, they would be affected by the proposals. Hearing, with testimony from a variety of affected parties and experts in both trade and, in particular, energy would also be a useful and constructive mechanism for exposing all of the issues that should legitimately be considered in fashioning a bill that makes a substantial change in our trade laws.

DEFINITION OF AN "UPSTREAM" SUBSIDY

The committee press release of October 12, 1983 discussed three alternative methods of determining the level of a subsidy granted by a foreign government. All of them deal with the term "controlled domestic price" on the part of the foreign government. In some countries it may be possible to establish a controlled domestic price; but in other countries we believe it is impossible to distinguish between a controlled domestic price and a price that is a natural advantage because of that country's unique natural resource position. For example, in the Middle East there are still very large surpluses of associated natural gas which have no market. This gas can be flared and wasted, or it can be sold locally at prices that are low enough to attract an industrial use. This appears to be a natural advantage rather than a controlled domestic price, particularly since it is not economically feasible to move that gas to the U.S. or elsewhere where an existing manufacturing market exists.

A similar case can be made for electricity which is generated from hydroelectric facilities. Many countries have used the natural advantage of their river resources to generate very low-cost hydropower. The government may set prices for the electricity which are low compared to fossil or nuclear-generated electricity, but subsidies are not necessarily involved. It is simply a question of low-cost resources being available. In most cases hydropower is like Middle East natural gas. Neither the electricity nor the water that generates it can be moved to an existing U.S. market.

DEFINITION OF A NATURAL RESOURCE OR BYPRODUCT OF A NATURAL RESOURCE

Another serious question is how to define a natural resource. The various legislative proposals address subsidies in terms of natural resources or byproducts of natural resources. One proposal also discusses the subsidization of "Materials". Almost anything can be considered to be incorporated into some other product that is then imported into the United States. The subcommittee draft bill would permit the administering authority to go upstream beyond the immediately preceding stage of manufacture or production upon a finding of substantial effect on the price of the merchandise being exported.

From the language circulated to date it would appear electricity could be classified as a byproduct of a natural resource. In the case of hydropower it is generated from water . . . the resource. It is also generated from fossil resources . . . natural gas, petroleum and coal. Since electricity is one of the major cost components in the electrochemical process used to make aluminum, one could even argue that aluminum is a byproduct of an energy natural resource.

We would like the opportunity to study suggested definitions of energy byproducts in depth in order to fully understand the implications of the legislation. We urge the committee to do the same.

U.S. VS. FOREIGN PRICES FOR ENERGY

The question of energy prices and international differences in energy prices is also very complex. The proposed legislation would cause duty to be imposed based on the "level of subsidy". In some proposals the level of subsidy is keyed in part to the difference between the price for the resource that is generally available to U.S. companies and the price of the resource in the foreign country. One problem is that in the United States there are a number of energy sources that have artificially high prices that are not the result of market factors. This is particularly true in the industrial sector.

In many cases U.S. industry is forced to pay artificially high, regulated energy prices in order to keep prices lower for residential users on the same utility systems. Natural gas is one example. In the Natural Gas Policy Act of 1978, industrial boiler owners were mandated to pay artificially high prices for natural gas that matched the fuel oil alternate prices. Further, a number of state regulatory commissions have adopted natural gas price schedules to industry based on alternate fuel values, marginal costs or inverted rates. All of these push natural gas to the industrial consumer much higher than any market-ordered cost. There would be serious implications if these prices were used as the basis for calculating subsidies.

Electricity prices present a similar problem. In jurisdiction after jurisdiction, industrial rates have been pushed to levels far beyond the utility's actual cost of service. The offsets or subsidies are then passed on to residential users. In fact, these U.S. practices have been one of the principal reasons several U.S. industries, including aluminum, are having worldwide competitive difficulties. In the opinion of Kaiser, the domestic problem may be far more serious than foreign government subsidies, particularly in electricity. The 1984 Bonneville power authority electric rate to direct service industries is an example. This rate has increased almost 800 percent in the last five years and is now at 26.8 mills per kilowatt hour. This forces the one-third of the U.S. primary aluminum industry located in the Pacific Northwest into a marginally competitive position in the world market. The offsets to that rate heavily subsidize other users.

The growing spread between U.S. industrial and foreign electricity prices is being further compounded by the cost of environmental controls. The proposed acid rain legislation is a good example. The pending legislation could raise electricity rates for one of Kaiser's key aluminum plants by more than 25 percent; thereby causing further damage to its international competitiveness. This, again, raises the question of how to determine a level of subsidy by a foreign government if a comparison to U.S. prices is to be the criterion. Should the cost of U.S. Government mandated environmental controls be part of a subsidy calculation?

ECONOMIC ADJUSTMENTS AND FOREIGN POLICY CONSIDERATIONS

There are several potentially adverse consequences that could result if trade legislation imposing additional countervailing duty on goods made with energy, or other natural resources having a subsidized price, were enacted and implemented without adequate time allowed for both governments and industries to plan and react.

First, there could be serious negative foreign policy implications. Countries that have established their pricing practices, investment strategies and other policies with respect to natural resources over the past decade could be immediately and adversely affected. In some cases it is questionable whether the affected countries could remain economically stable in the face of legislation having an immediate impact.

In particular, the United States has an interest in making certain its laws do not arbitrarily harm Third World Economies. Several of these countries have worked hard, along with U.S. partners, to effectively utilize what few natural resources thay have in developing their own economies and trade relations with the United States. In this regard, it should be noted LDC's presently account for 40 percent of U.S. exports and represent important growth potential for U.S. exports in the future.

Second, there are serious economic risks to many U.S. companies and U.S. consumers if the legislation were to be enacted in its present form. Many U.S. companies have planned and constructed facilities in foreign countries in return for certain economic incentives for locating there. These actions are in full accord with existing United States trade policies which encourage private investment, as opposed to U.S. Government assistance, as the preferred method for helping such countries with their economic development. If legislation were to be enacted which would suddenly subject the products being produced in such facilities to duty simply because of a natural resource cost advantage that had been freely negotiated in the past, considerable damage could be done. If legislation is eventually enacted, there should be a carefully designed phase-in period so that adjustments can be made on an orderly basis by the U.S. companies and host governments involved.

As pointed out earlier, change in trade policy and law must take into account the overall health and growth of the U.S. economy. Jobs, consumer prices and exports from the U.S. are three important parts of this equation. One area of immediate concern is the impact of this legislation on farmers and the cost of agricultural products. One of the products in question is fertilizer. Farmers have benefitted from having access to low-cost, imported fertilizers and would pay substantially more for these products if additional duty were imposed as envisioned by the proposed legislation. Any increase in the cost of producing food will be felt by the American consumer. It is advantageous to the farmer and the consumer to use low-cost fertilizers in the production of food. If the price of fertilizer is driven up by trade legislation, agricultural production could decrease with commensurate losses to the U.S. economy. The international competitiveness of U.S. agricultural exports and the resulting balance of payments consequences also must be considered.

As a final point, it is vitally important that any trade legislation be defensible, both generally and with our trading partners. It should be able to withstand international scrutiny. In the past, some trade legislation, although well intended, has resulted in serious trade problems. The creation and operation of the domestic international sales corporation is an example. Care should be taken to make certain that upstream subsidy legislation is GATT compatible and will not invite retaliatory action by foreign governments adversely affected.

In this statement, Kaiser has attempted to share with the Subcommittee on Trade some of the questions and concerns it has with the proposals to include "upstream" subsidies under the U.S. countervailing duty law. The agenda of this hearing and time constraints have precluded our addressing other proposed reforms to U.S. trade law. Because of the complexities of the numerous issues involved and the inter-relationship of the various laws, Kaiser respectfully urges the subcommittee to afford all interested parties the time reasonably necessary to fully and carefully assess all of the proposed reforms.

Without such a full and open debate, Kaiser has no alternative at this time but to oppose the inclusion of upstream subsidies under U.S. countervailing duty law.

STATEMENT OF THE LABOR-INDUSTRY COALITION FOR INTERNATIONAL TRADE [1]

The Subcommittee, in its consideration of reforming U.S. unfair trade practice laws, has decided to hold this hearing to examine whether two-tier pricing of government-owned natural resources constitutes an upstream subsidy. If so, a related issue is how such a subsidy should be measured. The Labor-Industry Coalition for International Trade ("LICIT") presents its views on these issues in this statement.

Earlier this year LICIT published a study called International Trade, Industrial Policies and the Future of American Industry. The report examined the trade and international competitiveness problems for American producers brought about by other governments' industrial programs and policies. One of the case studies in the report analyzed the industrial promotional policies for the petrochemical industry by the governments of Mexico and the U.S.S.R. A fundamental component of both the program in Mexico (state-owned company) and the U.S.S.R. (non-market economy) is the provision of natural gas to their domestic petrochemical company at prices substantially below export prices and world market prices. Since natural gas can comprise from 50 percent to 85 percent of the cost of producing petrochemicals like ammonia, ethylene and methanol, a significant reduction in the price of natural gas will substantially lower production costs for petrochemicals. Therefore, the Mexican and Soviet petrochemical companies have a significant advantage in price competitiveness in world markets.

The issue being examined by the Subcommittee is whether the price advantage enjoyed by the government-controlled petrochemical entities of Mexico and the U.S.S.R. is the result of a comparative advantage (relatively abundant supplies of natural gas) or the result of an upstream subsidy provided by the governments of these countries. LICIT believes that the price advantage here is clearly the result of an upstream subsidy provided by the respective governments.

There is no doubt that these two countries possess significant supplies of petroleum and natural gas. The issue is the discriminatory valuation of the gas by the two governments to subsidize domestic industrial activities that use natural gas intensively, particularly their petrochemical industries. The price available to domestic users is substantially below world market prices and export prices. Corporations outside of these two countries cannot purchase the natural gas at the low internal price. The internal price is set by government fiat, at a level substantially below prices established in world markets. The cost advantage to the Mexican and Soviet petrochemical producers on their final product is significant.

The U.S. countervailing duty law should be amended to provide that the two-tier pricing of natural resources by governments constitutes a countervailable subsidy. The subsidy should be calculated by taking the difference between either the export price and the restricted price or the world market price (generally available to U.S. producers) and the restricted price. If the subsidized resource is made "generally available" to industrial users, the countermeasures should be restricted to those industries where the subsidized resource has a significant effect on the total cost of production.

LICIT believes that this trade law reform issue and others that the Subcommittee is examining are very important. However, as we have already indicated to the Subcommittee in a separate letter, focusing on countervailing duty and anti-dumping laws alone is really not adequate. New authority and changes are also required in Section 301 and 201 of the Trade Act in order to round out and complete the actions of the Subcommittee so far. These additional changes were outlined in the letter sent to the Subcommittee members on October 3. LICIT hopes that the Subcommittee will continue to examine these additional proposals and react favorably to them.

---

[1] Submitted in behalf of Bethlehem Steel, Amalgamated Clothing and Textile Workers Union, Combustion Engineering, Inc., Communications Workers of America, Corning Glass Works, International Union of Electrical, Radio and Machine Workers, International Brotherhood of Electrical Workers, American Flint Glass Workers Union, The B. F. Goodrich Co., Industrial Union Department, AFL–CIO, Ingersoll Rand Co., International Ladies' Garment Workers Union, International Association of Machinists and Aerospace Workers, United Paperworkers International Union, United Rubber Workers of America, St. Joe Minerals Corp., United Steelworkers of America, W. R. Grace & Co., and Westinghouse Electric Corp.

Statement on Behalf of Leather Products Coalition,[1] Submitted by Stanley Nehmer, President, Economic Consulting Services Inc.

Introduction

This statement is being submitted on behalf of the members of the Leather Products Coalition, a group of trade associations and labor unions in leather-related industries. The products manufactured by these organizations include shoes, luggage, handbags, personal leather goods, work gloves, and leather wearing apparel.

The issue addressed in this statement is the bounties or grants to manufacturers of merchandise resulting from export restrictions (e.g., export taxes or embargoes) on inputs used in the manufacture of the merchandise. The particular input at issue is animal hides, the export of which has been restricted, in some cases embargoed, by countries such as Argentina, Uruguay and Brazil. Such export restrictions result in an artificially low domestic price for hides and the leather made from the hides, which ultimately benefits manufacturers of leather products in these countries (e.g., shoes, luggage, handbags, personal leather goods, work gloves, leather wearing apparel).

The circumstances relating to a subsidy on hides are quite similar to the circumstances contemplated by the Subcommittee in the natural resource subsidies. Alternatively, since hide export restrictions result in a lower price for inputs, this subsidy might be considered in the generic category of "upstream subsidies." While it is clear that this subsidy should be countervailed against, it remains unclear which section of the proposed law will cover it, natural resources or upstream subsidy. One suggested solution is to clarify the natural resources language to cover products such as hides. In any event, all appropriate measures should be taken to insure that the type of subsidy discussed in our statement is actionable under our countervailing duty law.

Foreign Export Restrictions on Hides Result in Subsidies to Foreign Manufacturers of Leather Products

Export restrictions on hides have been maintained by Uruguay, Argentina, and Brazil. These restrictions have taken various forms, including hide export embargoes and export taxes. The result is the same: an artificially low domestic price for hides and leather. The world market, by contrast, is faced with a reduced supply of hides and consequently higher hide and leather prices than would otherwise prevail.

Leather is the most important raw material input into leather products. The subsidy which results from hide export restrictions thus has a substantial price effect on both leather and leather manufacturers. As a result, the price of leather product exports is a "subsidized" price. This is perhaps most clearly evident in cases where leather product manufacturers maintain close relationships with the tanners, which is the case in some of the countries which restrict hide exports.

Notably, the Department of Commerce has agreed, in principle, to consider subsidies to manufacturers of leather products resulting from controls on hide exports as potentially countervailable: "The Department [of Commerce] will consider any possible bounties or grants to [leather] apparel manufacturers from an export tax on hides in the administrative review of the order." Leather Wearing Apparel From Argentina (48 Fed. Reg. 11481). See also Non-Rubber Footwear From Argentina (48 Fed. Reg. 19921). It is far from certain that Commerce will countervail in such cases in the absence of legislation covering this point.

Upstream Subsidies, Including Hide Export Restrictions, Should Be Included in Countervailing Duty Law

Upstream subsidies are addressed in Section 104 of the October 5, 1983 Subcommitte draft of the "Trade Remedies Reform Act of 1983," and in proposed new Section 771A to the Trade Agreements Act of 1979. An upstream subsidy is defined as a "government action . . . that is paid or bestowed by a country with respect to a product that is used in the manufacture or production of merchandise which is the subject of a[n] [countervailing duty] investigation." An export tax on hides meets this definition. The second criterion of the definition states that upstream subsidies are those that "result[s] in a price for the product for such use that is lower than

---

[1] Members of the coalition: Amalgamated Clothing and Textile Workers Union, AFL-CIO, Footwear Industries of America, Inc., International Leather Goods, Plastics and Novelty Workers' Union, AFL-CIO, Luggage and Leather Goods Manufacturers of America, Inc., United Food and Commercial Workers Union, AFL-CIO, and Work Glove Manufacturers Association.

the generally available price of the product in the country of manufacture, production, or export. . ." Clearly, this criterion may apply for hide export restrictions if such restrictions result in lower prices of leather to, for example, leather product manufacturers which maintain a close relationship to tanners, but do not result in lower prices to the general population of leather products manufacturers. The definition of upstream subsidies, as controlled by this second criterion, would not apply to an export restriction which results in a domestic price for the input that is lower than an export or world price but is a generally available domestic price. In this instance, an "adjustment of [the] generally available price" is necessary to offset artificial price depression by reason of any subsidy. This, too, is provided for in the proposed legislation.

Notably, a case in which an export restriction results in a domestic price for an input is lower than an export or world price, rather than a price lower than is generally available, is more analogous to a subsidy resulting from foreign government regulatory controls on natural resources. Although no legislative language has been proposed by the Subcommittee, the description of natural resource subsidies is relevant. The Subcommittee press release referenced authorization of "a countervailing duty against imports of a resource-based product if the resource is the subject of a government-price control scheme which sets a lower price for domestic use than for export action." Further, the controlled resource must constitute a significant portion of the resulting product's manufacturing cost. The situation described for hides would meet both of these criteria.

The Subcommittee has proposed three alternative measurements of the subsidy level: (1) the difference between the controlled domestic price and the export price; (2) the difference between the controlled domestic price and the lower of the export price or the price generally available to U.S. producers; and (3) the difference between the controlled domestic price and the "fair market value."

The Leather Products Coalition feels strongly that the pricing policies at issue, including export restrictions on hides, should be treated as subsidies, and at this time considers that the appropriate measure of the subisidy level needs to be decided, in consultation with the petitioner, on a case-by-case basis. In the case of export restrictions on hides, the most apppropriate measure would be the difference between the controlled domestic price and the world price for hides.

CONCLUSION

The Leather Products Coalition urges the Subcommittee, in its consideration of various subsidy practices such as two-tiered pricing schemes on natural resources and other "upstream subsidies," to recognize also the subsidy resulting from hide export restrictions. Appropriate language in the bill covering such situations should be included.

NATIONAL ASSOCIATION OF WHEAT GROWERS,
Washington, D.C., October 26, 1983.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C.

DEAR CHAIRMAN GIBBONS: This is to express the concern of the National Association of Wheat Growers regarding legislative proposals being considered by the Subcommittee on Trade which would change current countervailing duty law as it applies to "upstream subsidies."

As we understand proposals now before the Subcommittee, a new test would be introduced which would target the subsidized input used in the production of an export product. If a government subsidy were passed through to the export product, then the difference between the subsidized input and the value of the exported product would constitute a countervailable subsidy.

We believe that this proposal amounts to a radical change in trade policy which will increase energy-based production costs of the American farmer. Further, we recognize that the nations that would be struck by this policy change are now major markets for U.S. grain, and we believe that the proposed countervailing duty mechanism will lead directly to retaliation against U.S. grain trade. The Soviet Union and Mexico, two major markets for U.S. farmers are certain to fall in this category, since they are large producers of nitrogen fertilizer.

The U.S. grain industry and our farm export economy are based on the principle of comparative advantage. We fear that countervailing duty legislation under consideration will prompt other nations to "mirror" our action, and thereby eliminate the trade advantages that are vital to U.S. farmers and our national economy.

We urge your subcommittee to reconsider the proposals to change the application of current law as it applies to "upstream subsidies" to prevent sharp increases in farm production costs and to protect valuable markets for U.S. trade.

We appreciate your attention to our views, and we ask that this letter be made a part of the Subcommittee's October 20, 1983 hearing record on this subject.

Sincerely,

CARL SCHWENSEN,
Executive Vice President.

PETROLEOS MEXICANOS,
October 18, 1983.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, Committee on Ways and Means, U.S. House of Representatives, Washington, D.C.

DEAR MR. GIBBONS: Per your press release of October 12, 1983, we have been informed regarding your intention of holding a public hearing to consider various proposed amendments to the countervailing duty law designed to address the problem of two tiered pricing schemes established by foreign governments on natural resources. Furthermore, we are aware that testimony will be received from invited witnesses only, on Thursday, October 20, 1983, at 9:00 a.m.

You have also expressed that any interested person or organization may file a written statement for inclusion in the printed record, by submitting 106 copies of such document to Mr. John J. Salmon, Chief Counsel of the Committee on Ways and Means, during the course of the public hearing. Consequently, Petroleos Mexicanos, PEMEX, the company I have the honor to represent, avails itself of this opportunity to present its views on the matter.

PEMEX is a decentralized public agency of the government of Mexico, created by Decree of the Congress on the Mexican United States of June 7, 1938 and is the entity through whch the Mexican Government carries out the exploration and exploitation of the nation's hydrocarbon assets.

The principal purposes of PEMEX as set forth in the Organic Law of Petroleos Mexicanos, are the exploration, exploitation, refining, transportation, storage, distribution and first-hand sale of petroleum derivatives which be used as basic industrial raw materials and such other activities as are directly or indirectly related to the petroleum and petrochemical industries.

Under the Mexican Constitution and laws, production of petroleum, gas, refinery products and basic petrochemicals is carried out by a single state entity, PEMEX. In this way, the Mexican Nation has maintained control over the development and utilization of its hydrocarbon resources.

PEMEX is totally integrated in its production of petroleum, gas and petrochemicals, "from oil and gas extraction, refining and marketing, to the production, sale and export of basic petrochemicals, including ammonia."

Recently, PEMEX had to undergo an administrative investigation by the U.S. Commerce Department on account of a countervailing duty petition brought by protectionist domestic producers of ammonia in the United States. The argument for a monumental subsidy rested precisely on the so-called two tier pricing of natural resources; in this case, the difference between the export price of natural gas and the domestic price of such gas to produce ammonia.

Very correctly the U.S. Commerce Department decided there was no subsidy subject to countervailing duties when the domestic price of natural gas—although evidently lower than the export price was generally available to all the domestic industry, pointing out the difference to possible internal price discrimination.

The same ammonia U.S. producers, instead of challenging the administrative decision in the Courts, have gone to the legislative change effort, which we find extremely dangerous in that by vulnerating the right of nations over their national resources and of disposing them in a way that increases their comparative advantage, could invite similar actions. The United States should not forget that it exports 10 billion dollars 500 million to Mexico, per year, of petrochemicals based on regulated prices of natural gas.

The current definition of countervailable subsidy in U.S. law is a direct result not only of a long legal history but also of international agreements on such matter. The bills that have been introduced by trying to develop the new concept of upstream subsidies on the sale of natural resources to downstream producers will harm the United States and the rest of the world.

The substantive changes in the definition of subsidy are intended to broaden protection of U.S. domestic producers against import competition. The type of protection that would be provided by the revised subsidy definition raises a basic philosophical issue concerning economic development and international trade. Proponents of the bill apparently regard policies adopted by countries to regulate or organize their economies for development purposes as providing an unfair trade advantage.

However, the types of government practices that would be reached by the proposed amendments generally have not been considered unfair trade practices heretofore, either internationally or under U.S. legislation. Indeed, the fact that new legislation is being proposed to cover these practices demonstrates that the protection sought by these producers goes beyond traditional concepts of unfair trade.

The proposed legislation is essentially anti-development. It would tend to penalize countries for adopting programs intended to manage and guide their own economic development. Basically, the proposed legislation would inform developing countries that if they wish to continue trading with the United States, they should avoid certain types of management of their own economies, including measures that may be among the most effective channels of development for the particular country.

The development dilemma imposed by the expanded concept of "subsidy" is exemplified by Mexico's natural gas pricing policy, which is a target of the legislation. The bill seeks to treat as a subsidy a government regulated domestic price, if that price is lower than the export price for a raw material input into an exported product. The export price for Mexican natural gas sold to the United States, as approved by the United States government, is much higher than the regulated price of natural gas sold for industrial use within Mexico. This price differential reflects the very different levels of development between the United States and Mexico. The market price for gas sold in the United States results from the effects of the U.S. gas regulation scheme, in the context of a wealthy economy. In selling to the United States, Mexico properly receives the United States market price. Mexico presents an entirely different market for indigenous natural gas. Per capita income in Mexico is much lower than that in the United States, and the lower level of economic development of Mexico is reflected throughout the economy. Any effort to sell gas in Mexico at the U.S. market price would not only be unsuccessful, but would have extremely serious disruptive effects on the economy.

Industrial users of natural gas in Mexico are in no position to pay the U.S. price. It would be self-defeating for Mexico to attempt to charge the U.S. price for natural gas in Mexico, since this would seriously handicap the Mexican economy with respect to production for both domestic consumption and export. Nor would an attempt to charge the U.S. price in Mexico be an economically rational use of the resource. Natural gas is produced along with the production of oil, and unless captured or utilized, must be flared—that is, wasted. The amount of natural gas that Mexico can export is limited by transportation considerations and U.S. regulation of natural gas imports. Thus, unless sold in Mexico at prices the Mexican market can bear, huge amounts of Mexican natural gas would have to be flared—and given no economic use.

In the absence of an open-ended export market for natural gas, it should be apparent that the so-called "dual pricing" of natural gas by Mexico is dictated by economic realities. An effort to impose a uniform price on domestic and export sales would result either in waste of natural gas or, conceivably, export of natural gas to the United States at prices below the U.S. market price. Mexico should not be forced to accept either of these two alternatives. The first, unnecessary waste of a natural resource should be unthinkable. The second, sale to the United States at prices below the U.S. market price, probably would be opposed by U.S. natural gas producers and would not be approved by the U.S. Government. Even if approved, the United States should not coerce Mexico into selling natural gas at a price below the price offered by the market.

The antidevelopment philosophy of the proposed legislation is apparent also in the case of transportable raw materials that might be sold in the world market. The Mexican market can bear only a certain price level for the purchase of raw materials. When those raw materials are indigenously available in the country, they are part of the country's heritage and comparative advantage, and can be made available on terms consistent with the development level of the local economy. This price may be well below the price prevailing in international markets for the commodity, which is set basically by the demands of the industrialized countries. Treating as a subsidy the practice of making indigenous raw materials available to the local economy at prices consistent with local development, while also exporting into the world market at world market prices, conveys only one message to developing countries. That message is that developing countries must export their raw materials to the industrialized countries, rather than use their natural resource wealth to develop local industry.

The legislation would penalize countries for adopting totally rational and desirable development policies that are based, not on foreign assistance or largess from the international community, but rather on use of their own indigenous resources. Such legislation would operate directly against economic development goals that have been espoused and supported by the United States and virtually every other country in the world.

The message of the so-called "targeting" subsidy provision is the same. In the proposed legislation, the United States would be saying that developing countries cannot guide the development of their local economy if they wish to trade with the United States. Instead, developing countries must permit their economies to respond solely to the initiatives of the private sector, without regard to whether the fortuities of private sector investment advance the country's level of development. The United States should not use trade sanctions, which can be a powerful tool indeed to restrict development options available to developing countries.

It is recognized, of course, that the United States properly may take measures to protect domestic industry against unfair imports. However, "fairness" is a very subjective concept. What is notable about the proposed legislation is that it attempts to label as "unfair" practices that have not previously been considered to be unfair, either under international trading rules or under the legislation of the United States.

The philosophic departure of the present trade reform bill from prior trade legislation also is evident from the foreign investment rule that would be introduced into the definition of subsidy. The new subsidy definition would include, as a countervailable "targeting" practice, restrictions on foreign investment by the exporting country in its domestic economy. The apparent purpose of this provision is to put pressure on developing countries to permit U.S. companies to move their production from the United States to the developing countries, in order to benefit from the very comparative advantage attacked in other provisions of the bill. It is unusual that a trade law would be used to further investment by U.S. companies in production outside the United States.

While increasing the level of protection for domestic industries conceivably might result in some short-term benefit for those industries, the overall effect of the bill would seem to be contrary to the broader interests of the United States. First, any protection achieved for particular domestic producers would be at the expense of U.S. consumers as well as foreign producers. Second, by stifling exports from developing countries, the bill would necessarily reduce the foreign exchange earnings of those countries, thereby hurting their ability to service foreign debt (much of which is owed to U.S. banks) and to purchase U.S exports.

The United States consistently has supported the development of lesser developed countries, recognizing that such development enhances world security and benefits the United States both directly and indirectly. The present trade reform legislation, targeted as it is against development programs of developing countries, seems to be an unfortunate step backwards. While "trade, not aid" may not be a current development slogan, it nonetheless reflects a basic reality. Ultimately, the lesser developed countries will not be able to advance unless they are able to implement development strategies that seem appropriate in their national contexts and still maintain trade with the United States, which is the major developed country in the world. Simply labeling previously acceptable practices as "subsidies" does not make those practices unfair in the world trading context and should not be used as the basis for providing protection to the proponents of this subsidy definition.

Finally, the proposed legislation is clearly designed to change the rules of what constitutes a "subsidy" because the domestic anhydrous ammonia producers failed to obtain a countervailing duty on the basis of their petition filed last October against import of this product from Mexico. The legislation is "tailored" to prevent anhydrous ammonia and certain other exports from Mexico and, while couched in general terms, is clearly directed against Mexican imports which have an energy component. To take such a step against the immediate neighbor of the United States, which is a principal trading partner, in order to accommodate domestic producers who failed in their objectives under existing rules is hardly tenable in relations between neighbors. For this reason alone, as well as the more general ones cited above, the bill should be rejected.

PEMEX is sending around 800 thousands barrels of oil per day to the United States. For 13 consecutive months we have been the prime source of foreign hydrocarbons to your country.

Of course, we aspire not only to send crude oil, but also refined products and petrochemicals as well, particular because our reserves, classified as the fourth largest in the world at 72 billion barrels, give us a natural comparative advantage to—sell in the U.S. market.

On the other hand, Mexico is undergoing and overcoming a severe financial crisis through a very severe austerity program. It is in the interest of both our countries that we are able to service our debt and maintain a dynamic market, the third largest for the United States. Only by exporting those goods where we have a clear advantage, can we continue to be the promising 20 billion dollar market for your products.

Sincerely yours,

ALFREDO GUTIERREZ KIRCHNER,
General Representative,
New York and Washington.

STATEMENT OF SOUTHEASTERN LUMBER MANUFACTURERS ASSOCIATION

The Southeastern Lumber Manufacturers Association (SLMA) is a trade association comprised of more than 400 lumber manufacturing companies in 12 southeastern states. Each of its members employs 500 or fewer persons, and so are considered small businesses by the Small Business Administration and the forest products industry. The Association was formed in 1962. Its headquarters are in Forest Park, Georgia.

SLMA welcomes the attention of this Subcommittee and its chairman to the problems of an international trading system in which not all competitors are playing by the same rules. SLMA, and, indeed, the entire forest products industry, have a long history of favoring international trade. But we firmly believe that international trade must be fair as well as free. Unfortunately, our association and other members of the U.S. lumber industry are being victimized by an unfair trade situation.

Imports of softwood lumber from Canada steadily increased over the past two decades to the point where Canadian lumber now accounts for one third of all lumber sold in the United States. In Georgia, our association's home state and a principal lumber producing state of the Southeast, the Canadian share of the market is well over 50 percent. In Florida, it is approximately 60 percent.

Canadian mills are typically less efficient than U.S. mills. Canadian mills obviously are located much farther from our home market areas than we are. Canadian labor costs are typically more expensive than our labor costs. Why, then, in spite of these comparative U.S. advantages, have Canadian mills been able to take away more and more of our markets? Because almost all the timber in Canada is owned by the provincial governments of Canada, who provide it to Canadian mills for far less than its fair value.

The United States is the market for half of the lumber produced in Canada. The Canadians have therefore taken whatever steps they believe are necessary so they can underprice U.S. lumber and continue to expand their share of the U.S. market.

As a result, in Atlanta, for example, we find numerous developments of houses ranging in price from $50,000 to $200,000 which are being built completely of Canadian lumber. Our association's 14 mills in Florida, who sell most of their production right in Florida, are losing sales to lumber brought in all the way from Canada. In fact, a sizeable lumber manufacturer in Florida just joined SLMA because of its activities in trying to confer this Canadian incursion.

Because of our concern with the Canadian lumber problem, we joined in the Spring of 1982 with trade association and companies both large and small and from every major producing region of the United States to form the United States Coalition for Fair Canadian Lumber Imports.

We were impressed with the intent of Congress to provide through the 1979 Trade Act Amendments a fair, expedited, and non-political means to resolve trade problems such as ours. We believed the new countervailing duty process was perfectly suited to our situation because the Canadian governments were providing a subsidy to Canadian manufacturers in the form of bargain-price raw material which resulted in a easily documented injury to the United States industry. Ours was the largest countervailing duty case ever brought, involving some $1.7 billion worth of imports annually.

The U.S. International Trade Commission unanimously found in its preliminary determination that there was a reasonable indication of injury to the U.S. industry as a result of the imports from Canada.

The International Trade Administration of the Department of Commerce, however, determined both preliminarily and finally that only a de minimis level of subsidies flow from the Canadian governments to the Canadian manufacturers. Most importantly, the ITA held against our allegations that the Canadian method of providing standing timber to the manufacturers constituted a subsidy.

SLMA and the U.S. Coalition are extremely troubled by a number of points concerning the manner in which this case was handled by the Department of Commerce. We believe the intent of Congress was thwarted. We hope that the Subcommittee and ultimately the entire Congress will reassert its intent in a manner so clear that it cannot be evaded administratively. Without attempting to reargue the entire case for the Subcommittee, we do want to list for you some examples of our concerns with the way this case was handled.

I. Congress clearly intended that the ITA and ITC, while reaching decisions based on the merits of cases, also should take on a role of assisting U.S. industry in pursuing and presenting countervailing duty cases. We found the ITC both eminently fair and cooperative. At the Department of Commerce, however, the attitude seemed different. For example, Secretary Baldrige assured the Canadian ambassador that if a preliminary decision were unfavorable to the Canadians, the Department would cooperate with the Canadians in bringing the matter to the attention of the General Agreement on Trades and Tariffs (GATT). However, the preliminary determination was unfavorable to the U.S. industry. We sought review of two legal questions at the U.S. Court of International Trade. Instead, of cooperation, the U.S. industry was met by intransigence and procedural stonewalling on the part of the Department of Commerce and its attorneys, who openly consorted with attorneys for Canadian industry during the court case.

II. Determinations on countervailing duty cases typically are delegated to the Deputy Assistant Secretary for Import Administration. In this case, however, Secretary Baldrige personally made the decision on the key subsidy issue in this case. At a disclosure meeting with the ITA following publication of the preliminary determination, the Coalition was formally told when Secretary Baldrige made that decision. It is interesting to note, however, that the staff memorandum providing the rationale for one of the three key elements of the Secretary's decision was not prepared until after he made the decision. Despite the Department's denial, we remained convinced in our minds that the decision was a political decision based on strong protests from Canada.

III. The Department of Commerce narrowed the plain language of the statute in finding against the U.S. industry. The phrase "assumption of cost" in the statute is not qualified or limited in either the statute itself of the legislative history. The Department, however, interpreted this wording to mean only assumption of cost of a pre-existing contractual obligation or obligation to the government.

IV. A major issue in the case was how to determine the value of the standing timber provided by Canadian governments to Canadian manufacturers. The Department refused to utilize the U.S. market as a commercial benchmark although the lumber products at issue were sold into a common U.S. market. The Canadian value is nominally based on that market, and there is no private market within Canada available for comparison. This decision in part adopted false arguments advanced by the Canadians. At the disclosure conference following the preliminary determination, the Department of Commerce official who wrote the preliminary determination was asked how she could have ignored plain and verifiable submissions by U.S. industry contradicting the Canadian arguments. The official showed no awareness of this elementary and central information. Although the Department of Commerce spent numerous staff days in Canada during the case, it refused until long after the preliminary determination to make any field visits to U.S. industry areas along the Canadian border for the purpose of comparing cross-border timber prices.

V. Congress provided an interlocutory appeal procedure for countervailing duty cases. The preliminary determination against the U.S. industry contained three elements: two of them legal, and a third factual point which need not have been reached in light of the two legal decisions. The Coalition sought review of the legal points in the Court of International Trade so that if the Department of Commerce were reversed, the far more complex factual issue could be further argued in advance of a final determination. The Court, however, ruled that all issues from the preliminary determination had to be appealed. We do not believe Congress intended this result.

In light of our experience, we believe further revision of our trade laws is necessary. We were probably naive in expecting that a process designed by Congress specifically to be nonpolitical could actually operate nonpolitically on a very major case such as ours. Since it now is evident to us that politics will play a role in any major decision affecting lumber imports from Canada, we believe it is appropriate for the Subcommittee to consider this issue, and we look forward to working with you toward a resolution that promotes fair trade, not merely free trade. Certainly the need for action is urgent, because Canadian market penetration is up 10% just since the time our countervailing duty petition was filed. In light of our experience, we believe the Committee should consider the following actions:

1. Reaffirm previously expressed congressional intent by clarifying for the administrative agency the meanings of the terms "assumption of cost" and "specific industry or group of industries" in the statute. Attached is a copy of the Coalition's brief to the Court of International Trade which includes detailed arguments against the Department of Commerce's interpretation.
2. Specify that it is appropriate to consider a U.S. commercial benchmark in determining the value of a subsidy when there is no private market benchmark within the subsidizing country and the value of the subsidized article is significantly based on its value in the United States. Attached to this brief is a copy of the Coalition's submission to the Department of Commerce concerning commercial benchmark.
3. Clarify the interlocutory appeals procedure on countervailing duty cases so that controlling questions of law can be ruled upon by the Court prior to a final subsidy determination. This would promote efficiency in the handling by both the agency and court of the typically far more complex factual issues in a case.
4. Finally, Congress should consider some more direct route toward resolving the immediate problem of subsidized lumber imports from Canada that threaten to overwhelm the U.S. lumber industry. We do not at this point suggest whether a quota system, a tariff, a marketing agreement keyed to product demand, or some other mechanism would be most appropriate. We do insist, however, that some action must occur soon.

STEPTOE & JOHNSON,
Washington, D.C., October 12, 1983.

Hon. SAM M. GIBBONS,
Chairman, Subcommittee on Trade, House Committee on Ways and Means, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSMAN GIBBONS: I am submitting this letter in response to the request for comment on the Trade Subcommittee's proposal to impose countervailing duties on products which incorporate natural resource cost inputs supplied to the exporter at prices less than the export price for the resource in question.

As I think you are aware from my previous testimony before this Subcommittee, I have a continuing concern about the general problem of upstream subsidies, and I fully support the Committee's proposal to clarify the application of the countervailing duty law to upstream, as well as direct, subsidization. I and my firm also have had considerable experience in cases dealing with allegations that major cost inputs are furnished below "real world" prices. In one instance, we represented U.S. nail producers who were injured by imports of Korean nails which benefitted from wire rod obtained from a government-owned producer at a below-cost price. We have also been involved in cases which have included allegations that low-priced natural gas was used to manufacture the exported product. In one of those proceedings, we represented Occidental Chemical Corporation in connection with its imports of ammonia from the U.S.S.R. In another case, we are representing a wire rod producer in the Republic of Trinidad and Tobago, where natural gas provides a low-cost source of energy. From my experience in these proceedings, I have developed some fairly definite views on what is, and what is not, "unfair" in the area of cost inputs. In my view, the approach to this problem taken by the "natural resource" section of the Subcommittee's proposals is the wrong approach, is contrary to GATT and U.S. trade policy, and misconceives the nature of the problem.

The basic aim of American trade policy has been, and should continue to be, to eliminate, rather than increase, the barriers to free trade. This means that U.S. law, in keeping with international trading rules and agreements, should ensure that companies with natural cost advantages—better technology, or cheaper labor or raw materials—are not underpriced by higher-cost producers which dump their products or which receive subsidies to lower their otherwise-high cost of production. If the United States goes beyond this principle, and imposes barriers to imports which are inconsistent with the recognized international trading rules, other countries are likely to retaliate against our exports, and the world trading system will begin to back away from the free trade policies which have served so well over the last four decades.

Legislation which is directed at imports from developing countries, or at the development strategies of those nations, should be viewed with particular caution. The developing countries constitute the fastest-growing markets for U.S. exports. It is essential that their exports be maintained and increased in order for them to continue buying American goods and to pay off their heavy indebtedness. Legislation which restricts artificially their ability to sell in the United States is contrary to those goals. Moreover, such legislation creates the danger that those nations would begin to view the U.S. as an unfriendly trading partner, and thus reduce their purchases of U.S. goods in favor of imports from other countries.

These general considerations and the more specific problems discussed below lead me to oppose the proposed natural resource provision in your legislation. I view this provision as special-interest legislation, aimed at protecting the interests of a small group of domestic ammonia producers.[1] The provision is inconsistent with the principles of U.S. trade policy.

The basic concept of this proposal is to prevent foreign governments from providing cost inputs (particularly natural gas) to their domestic producers at a price which—although not below the cost of producing that input nor below the price at which the input is generally available to producers within that country—is below the price at which that input is exported form the country in question. This concept of "unfairness" has nothing to do with established concepts of countervailable subsidies.

Historically, based upon the theory of comparative advantage, the United States has encouraged the developing world to make use of its raw material (and labor) cost advantages to increase its exports, thereby earning the foreign exchange with which to buy goods and services from the developed nations, including the United States. This policy is essential to the economic growth and development of LCDs. If LCDs are prevented from taking advantage of their lower cost of producing natural gas and other raw materials, they will have no means of competing in world markets. Their exports will fall off; and with that decline in exports will come a reduction in their purchases of U.S. and other developed-country goods. Further, these countries' ability to repay their large indebtedness to Western banks will be placed in jeopardy.

It is not readily apparent why there is anything "unfair" about the practice against the natural resource proposal is directed. If a foreign country has a lower cost of producing a raw material, why should its manufacturers and exporters not benefit form that lower cost? The fact that the raw material in question could be exported at a higher price on world markets does not seem relevant. In the United States, for example, a number of ammonia producers in the Gulf Coast region have access to natural gas which—because of long-term contract pricing—is available to them at a cost substantially below the now-prevailing market price for natural gas. It is not considered an "unfair practice" for those producers to use that natural gas to make ammonia instead of reselling it as natural gas.

In addition, this concept of "unfairness" could easily be used against U.S. exports. For example, European and Japanese trading partners could argue that U.S. natural gas exports (e.g., to Japan) are at a higher price than the average price of natural gas sold internally. Indeed, a variety of U.S. exports would be subject to retaliation if the same rule is applied against us.

The natural resource provision would also place the producers of raw materials in foreign countries in an untenable position. Under the present antidumping law, they are committing an "unfair practice" if they export the raw material in question at a price lower than the domestic price for that material, i.e., dumping. Yet under the natural resource proposal, such producers would also be committing an "unfair practice" if they were to export their raw material at a price higher than the price charged in their domestic market. This sort of "damned if you do and damned if you don't" legislation has no place in American trade policy.

Further, foreign-owned producers are not the only recipients of the low-price natural resource inputs of which the bill complains. Some foreign subsidiaries of U.S. companies also receive hydrocarbon and other material resource inputs at these so-called "preferential" prices. If a proposal excludes from coverage products imported into the United States from foreign subsidiaries of U.S. firms which benefit from these low hydrocarbon prices, such a change would create an incentive for U.S.

[1] This legislation would also have the effect of increasing fertilizer costs to the American farmer.

firms to establish processing plants abroad. This in turn would obviously have adverse effects on United States employment.

There is yet another problem with this proposal. Because foreign countries often place an export tax on natural resource exports, many countries would be subject to countervailing duties under the natural resources provision. The internal price of these resources would be lower than their export price (at least by the amount of the export tax).

It should also be recognized that this concept of unfairness is inconsistent with U.S. obligations under the General Agreement on Tariffs and Trade ("GATT"). The GATT forbids the imposition of antidumping or countervailing duties unless there is a finding of either dumping or subsidization as defined in the Antidumping Code or the Code on Subsidies and Countervailing Measures. Neither of those Codes permits imposition of duties on the basis of furnishing to domestic producers inputs at prices lower than the export prices of those inputs.

Because of the shortness of time before your hearing on this subject on October 18, I am providing copies of this letter directly to the other members of the subcommittee.

Sincerely yours,

RICHARD O. CUNNINGHAM.

TRADE REFORM ACTION COALITION,
Gastonia, N.C., October 18, 1983.

Hon. SAM GIBBONS,
Chairman, House Ways and Means Committee, Subcommittee on Trade, Longworth House Office Building, U.S. House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: The Trade Reform Action Coalition ("TRAC"; membership list attached) is in this letter responding to your request for comments on the Subcommittee's October 5 draft bill, "Trade Remedies Reform Act of 1983."

TRAC is pleased that you have taken the leadership in bringing about much needed reform in our antidumping an countervailing duty laws. We are grateful to you for your efforts. TRAC finds much that we like in the Subcommittee draft. However, the draft contains several provisions that we would like to see changed and does not deal with several matters that we would like to see addressed.

TRAC continues to believe that there is a present need to review and revise sections 201, 301 and the Revenue Act of 1916 in connection with comprehensive trade remedy reforms. With respect to the more limited reform of the antidumping and countervailing duty statutes, Title I of H.R. 4124, which we support, contains a number of additional recommendations (for example, the elimination of settlement authority under 19 U.S.C. Section 1617) beyond those covered in the Subcommittee draft. We believe these proposals deserve the consideration of the Subcommittee members.

Specifically, in regard to the Subcommittee's draft, we are particularly concerned about the following provisions:

1. INJURY

Current law provides that cause of injury is to be determined by looking at the effects of dumped or subsidized imports. The Subcommittee draft would change this so that consideration would be given not only to the volume of dumped or subsidized imports but also to the margin of dumping or the level of subsidization. This proposed change would go in the opposite direction from the trade law reform character of this bill. As suggested by a representative from the ITC General Counsel's Office at an earlier informal mark-up, this proposal would further complicate the already complicated injury determinations. We believe it would also be very harmful to the interests of injured domestic petitioners in cases where the margin of dumping or the level of subsidization is moderate, since the very existence of subsidized or dumped imports carries with it the inherent effect of injury. Furthermore, there is nothing in the GATT that would require this change to be made. We strongly recommend that section 104(a)(2)(A) on page 14 of the bill be deleted and a new provision added that would codify ITC practice.

2. SETTLEMENTS

TRAC applauds the Subcommittee bill for seeking the elimination of the export tax offset as a means of settling countervailing duty cases. This provision has never worked properly and has been grossly unfair to domestic petitioners.

However, when dumping and countervailing duty cases are politically sensitive, other kinds of settlement agreements can provide our government with an appropriate and necessary alternative to the imposition of antidumping or countervailing duties. In many instances, duties would effectively foreclose the offending foreign products from the U.S. market. Settlements permit foreign products to continue to enter the U.S. market, but at reduced levels or with reduced margins of dumping. Instead of narrowing existing settlement provisions, as section 103 of the Subcommittee bill would do, these provisions should be expanded to permit quantitative suspension agreements in antidumping as well as in countervailing duty cases, and revised so that they require the consent of the petitioner.

Further, the Secretary of Commerce should be provided with negotiating and enforcement authority with respect to both antidumping and countervailing duty settlement agreements whose implementation would be conditioned upon the withdrawal of a pending petition and the resulting termination of the investigation. If desired, the Secretary could be directed to evaluate proposed settlement agreements in terms of the overall national interest, including foreign relations considerations and interests of domestic producers and consumers. The failure to provide a workable escape valve in the form of practical settlement provision will result in strong pressures on the Commerce Department to come up with negative determinations in cases where affirmative determinations would result in the politically unacceptable (to the Administration) imposition of duties. The choice for injured domestic petitioners in politically sensitive cases is frequently between no relief and partial relief under a settlement agreement.

3. NON-MARKET ECONOMY DUMPING

The current law relating to the determination of dumping margins with respect to products from non-market economies is admittedly awkward. Since the concept of dumping is difficult to apply to non-market economies, costs and prices do not have the usual meaning. Current law directs that costs be constructed by reference to a surrogate free market economy at a comparable level of development. The Subcommittee proposal would change the law so that non-market producers could sell in the U.S. market at a price equal to the weighted average free market price in the U.S. This is a significant improvement over an earlier lowest price proposal. However, the weighted average price could be difficult to arrive at administratively. In addition, even this proposed pricing standard could provide a "safe harbor" for dumping and put non-market producers in a more favorable position than high-cost free market producers. For example, an inefficient producer of widgets in Bulgaria whose cost of production is $100 per widget could, under this proposal, sell in the U.S. at a dumped price of $90 per widget if the weighted average free market price in the U.S. was $90. If section 105 and the weighted average pricing standard is retained in the bill, it should at least be modified so that it applies only when an economy as a whole is non-market instead of when a sector in question is non-market. In the near future, we hope to have an opportunity to comment further on this proposed pricing standard.

4. INTERMEDIATE APPEALS

Current law permits appeals from Department of Commerce and U.S. International Trade Commission determinations to the U.S. Court of International Trade at several logical points in antidumping and countervailing duty proceedings. This protects both petitioners and respondents, who would otherwise have to wait until their vital economic interests were severely harmed to take an appeal after a final determination. Congress had good reason in the 1979 Trade Agreements Act to permit intermediate appeals. Section 109 of the Subcommittee bill would eliminate the right to take intermediate appeals. The right to take intermediate appeals should be preserved at key procedural points.

TRAC appreciates the opportunity to comment on the Subcommittee's draft bill. However, we are very concerned with the provisions identified in this letter, as well as with the important matters covered by H.R. 4124 that are not dealt with in the Subcommittee's draft. Our shared goal is legislation that provides fully for trade law reforms which are desperately needed. We are available to work with the Subcommittee and its Staff to that end.

Sincerely,

JIM H. CONNER,
Chairman.

Enclosure.

MEMBERS OF THE TRADE REFORM ACTION COALITION (TRAC)

An alliance of U.S. companies, trade associations, unions and workers in the chemicals, color televisions, fiber/textile/apparel, footwear, leather goods, metal-working, nonferrous metals, and steel industries.

AMERICAN FIBER, TEXTILE, APPAREL COALITION (AFTAC)

AFTAC is a coalition of 18 trade associations and two labor unions representing the fiber/textile/apparel complex of the United States. It evolved for the purpose of representing these industries in issues of international trade.

The coalition is representative of an industry with facilities in 50 states, with employment totaling 2.4 million and sales accounting for $105 billion.

AFTAC MEMBERS

Amalgamated Clothing & Textile Workers Union, American Apparel Manufacturers Association, American Textile Manufacturers Institute, American Yarn Spinners Association, Carpet & Rug Institute, Clothing Manufacturers Association of America, International Ladies' Garment Workers' Union, Knitted Textile Association, Luggage & Leather Goods Manufacturers of America, Man-Made Fiber Producers Association, Inc., National Association of Hosiery Manufacturers, National Association of Uniform Manufacturers, National Cotton Council of America, National Knitwear Manufacturers Association, National Knitwear & Sportswear Association, National Wool Growers Association, Neckwear Association of America, Northern Textile Association, Textile Distributors Association, Inc., and Work Glove Manufacturers Association.

AMERICAN IRON AND STEEL INSTITUTE (AISI)

AISI is the principal trade association representing the United States steel industry. Its 61 domestic member companies produce 87 percent of the raw steel in the United States at facilities in 39 states.

In 1982, total sales were $52.3 billion and employment was 446,000.

COMMITTEE TO PRESERVE AMERICAN COLOR TELEVISION (COMPACT)

Compact is an unincorporated association comprised of three manufacturers and 11 labor organizations which represents the overwhelming majority of production and workers in the domestic color television industry.

Compact members employ approximately 18,000 people in 18 states and account for total sales of $4.5 billion.

COMPACT MEMBERS

Allied Industry Workers of America, International Union, American Flint Glass Workers Union of North America, Communications Workers of America, Corning Glass Works, Glass Bottle Blowers' Association of the United States and Canada, Independent Radionic Workers of America, Industrial Union Department, AFL–CIO, International Association of Machinists, International Brotherhood of Electrical Workers, International Union of Electrical, Radio & Machine Workers, Owens-Illinois, Inc., United Furniture Workers of America, United Steel Workers of America, and Wells-Gardner Electronics Corp.

GROUP OF 33 (AD HOC LABOR-INDUSTRY TRADE COALITION)

The Group of 33 is an ad hoc labor-industry trade coalition formed in 1978 to advocate changes in import trade remedy laws, with particular focus on the Multilateral Trade Negotiations, subsidies code and 1979 Trade Agreement Act.

The 28 industry trade associations and five labor unions that make up the Group of 33 represent a wide diversity of industries which include footwear, leather products, chemicals, lead and zinc, textile machinery, industrial equipment, various textile and apparel products, and agricultural products.

GROUP OF 33 MEMBERS

Amalgamated Clothing & Textile Workers Union, AFL–CIO, American Apparel Manufacturers Association, American Federation of Fishermen, American Mushroom Institute, American Pipe Fittings Association, American Textile Machinery Association, American Textile Manufacturers Institute, American Yarn Spinners

Association, Association, of Synthetic Yarn Manufacturers, Bicycle Manufacturers Association of America, Inc., Cast Iron Soil Pipe Institute, Clothing Manufacturers Association, Copper and Brass Fabricators Council, Inc., Footwear Industries of America, Inc., Industrial Union Department, AFL-CIO, International Ladies' Garment Workers' Union, AFL-CIO, International Leather Goods, Plastics & Novelty Workers Union, AFL-CIO, Lead-Zinc Producers Committee, Luggage & Leather Goods Manufacturers of America, Inc., Man-Made Fiber Producers Association, National Association of Chain Manufacturers, National Association of Hosiery Manufacturers, National Cotton Council, National Handbag Association, National Knitwear & Sportswear Association, National Knitwear Manufacturers Association, Northern Textile Association, Scale Manufacturers Association, Inc., Synthetic Organic Chemical Manufacturers Association, Textile Distributors Association, United Food and Commercial Workers International Union, AFL-CIO, Valve Manufacturers Association, and Work Glove Manufacturers Association.

METALWORKING FAIR TRADE COALITION (MFTC)

The MFTC is a coalition of 27 trade associations representing the U.S. metal parts industries that joined together in 1982 to seek government cooperation and action to assure fair trade between the United States and its world trading partners.

MFTC members have operations in 43 States with employment totaling 1.4 million and sales of $75 billion.

MFTC MEMBERS

Alliance of Metalworking Industries, American Cutlery Manufacturers Association, American Pipe Fittings Association, American Metal Stamping Association (Washer Div.), American Die Casting Institute, American Wire Producers Association, Association of Die Shops International, Cast Metals Federation, Cutting Tool Manufacturers Association, Expanded Metal Manufacturers Association, Forging Industry Association, Hand Tools Institute, Industrial Fasteners Institute, Industrial Perforators Association, Inc., Iron Castings Society, Metal Treating Institute, National Screw Machine Products Association, National Tooling and Machining Association, National Foundry Association, National Association of Chain Manufacturers, Non-Ferrous Founders' Society, Steel Founders' Society, Steel Plate Fabricators Association Inc., Tool & Die Institute, U.S. Fastener Manufacturing Group, Valve Manufacturers Association, and Welded Steel Tube Institute.

STEEL SERVICE CENTER INSTITUTE (SSCI)

SSCI is a trade association representing almost 500 North American companies in the steel industry, with 900 service centers in industrial areas. Service centers are divided into three types: industrial steel service centers, merchant products distributors and oil country jobbers. Approximately 124 steel producers are associate members.

With total sales of $20-22 billion, SSCI members employ 120,000 people in 49 States.

STATEMENT OF GERARD J. VAN HEUVEN, ON BEHALF OF UNITED STATES-MEXICO CHAMBER OF COMMERCE

UTILIZING ABUNDANT NATURAL RESOURCES TO IMPROVE DEVELOPING COUNTRY ECONOMIES: A SOVEREIGN RIGHT OR UNFAIR BENEFIT?

I am Gerard Van Heuven, Executive Vice President of the U.S.-Mexico Chamber of Commerce. The Chamber is a non-profit organization serving many of the larger U.S. companies operating in Mexico and over 180,000 Mexican firms, many of which are involved in trade with the United States. In my capacity with the Chamber, I am in a rather unique position both to understand the manner in which the proposals before the Subcommittee will affect U.S. trading relations with Mexico and to convey the view of the companies most directly affected by those proposals. I should preface my remarks by observing that it is apparent from both the comments already heard by this Subcommittee and the wording of the proposals themselves, that these proposals are largely directed against Mexico and its government-owned oil company, Petroleos Mexicanos, popularly known as PEMEX. In this light, I will primarily confine my statement to a discussion of the severe implications for U.S.-Mexico trade raised by the proposals and the compelling significance those implications have in the world trading framework.

The specific "upstream" subsidy provisions before the Trade Subcommittee seek to impose countervailing duties on imports that are produced from low-cost, government-owned or controlled natural resources. The purpose of such action, as stated in the Trade Subcommittee's October 19 press release, is to resolve the "problem of two-tiered pricing schemes" which "generally involve a rigidly controlled high world price for the resources coupled with a domestic price that is a mere fraction of the world price." Certain members of this Subcommittee, and many of those testifying before it, would have us believe, through innuendo and certain conclusory and unsubstantiated statements, that the government of Mexico administers such a two-tiered scheme. As more fully set forth below, such statements are erroneous and contrary to established fact. It is clear, moreover, that the subject proposals are violative of the most fundamental principles of international trade policy and threaten to severely undermine U.S. relations with Mexico and other developing countries.

A. Proponents of the "upstream" natural resource subsidy proposals have misrepresented the energy policies of Mexico

The statements purporting to portray the subject practices of Mexico seriously misrepresent the reality of Mexico's energy pricing policy. That policy is a simple and uniform one based upon two compelling premises: (i) Mexico is a developing country which is in desperate need of widespread industrial development; and (ii) one of the few advantages available to Mexico in pursuing its economic development is its abundant hydrocarbon reserves.

Mexico's energy policy is implemented by PEMEX, which is a special government organization created by the Decree of Congress of United Mexican States of June 7, 1938. The Mexican government carries out the exploration and exportation of the nation's hydrocarbon assets through PEMEX, and accordingly the principle purposes of PEMEX are the exploration, exploitation, transportation, refining, storage, distribution and sale of petroleum, natural gas and refined products, as well as the manufacture, storage, transportation, distribution and sale of petroleum derivatives used as basic industrial raw materials.

In conducting the sale of hydrocarbon products, and in particular the natural gas which is the primary concern of those who have proposed "upstream" subsidy countermeasures, PEMEX administers a uniform price program for all domestic users. PEMEX does not provide a separate framework for export sales of its products. Within Mexico, there are two categories of energy prices established by PEMEX, one for industrial use and another for residential use. Both of these prices are set by the Direccion General de Precios of the Secretaria de Comercio. All energy sold for residential, commercial and service uses are sold at a standard residential use rate. All energy sold for industrial purposes is subject to uniform industrial use prices. All industrial users of energy within Mexico, both U.S. and Mexican firms, obtain it at the same price. The pricing program administered by PEMEX is not designed, and does not serve, to stimulate export sales over domestic sales, nor is it provided to any single specific enterprise or industry.

Mexican energy is not set at an "artificially low" price, as the proponents of the instant proposal seem to suggest. Indeed, PEMEX derives a profit on its domestic sales. Neither PEMEX nor any other Mexican entity set or establish a world price for its energy. If a foreign country wants to purchase oil from Mexico, Mexico looks to the current OPEC price. Mexico will not sell all of its oil to the world at a price it grants to its private sector. The new legislation therefore demands that a sovereign nation must increase domestic prices of its natural resources to U.S. levels, or suffer a countervailing duty. I argue that this action is profoundly wrong, from a policy standpoint, a legal standpoint, and a practical standpoint.

The countervailing duty laws were written to redress inequities created when governments intervene to create preferential advantages which nature does not confer. They were not written to "level out the playing field" simply because an industry in the U.S. must pay more for a commodity than must an industry in a foreign country.

The bottom line in Mexico is that oil is cheap. It has what many claim to be the the third largest oil reserves in the world after Saudi Arabia and the Soviet Union. While the United States happens to have drilled 2.5 million oil and gas wells, thereby discovering most of the inexpensive fields and reservoirs within its borders, Mexico has drilled only 30,000 wells. Mexico should in reality be compared to the U.S. of 30 years ago. Having taken advantage of the intervening period of its own 30 years of development, the U.S. should not now attempt to turn back the hands of time by using the countervailing duty law to compensate for its loss of inexpensive fuel. Mexico's advantage is the advantage of nature, not of an unfair subsidy practice. The United States has itself engaged in many similar practices based upon resources which are particularly abundant within its own borders.

B. The proposals are in clear violation of GATT and the GATT subsidies code

The proposals before this Committee, clearly ignore the international trade framework which has been carefully negotiated between the United States and our major trading partners. The use of subsidies which is the fucus of these proposals is hardly a noval international trade issue. It has been debated extensively in multilateral trade negotiations dating back thirty years and more. Indeed, probably no other trade issue has been debated more extensively than the role of official subsidies and other governmental economic programs in the international economy. Those extensive efforts have clearly defined those categories of subsidy which may be considered countervailable under international trade rules. The expansion of those categories sought by the proponents of the instant proposals goes far beyond those permitted categories and accordingly violates the GATT rules.

1. Such proposals to penalize industry-wide assistance are against basic GATT principles.—Nothing is more basic to the trade relief framework which has been so arduously developed during long years of negotiation between the United States and its primary trading partners than the right of nations to promote and foster the development of their respective economies in a manner consistent with their unique heritage and social exigencies. In weighing that premise and the broader premise of national sovereignty, it is axiomatic that the United States and every other country of the world has the fundamental right to choose its economic destiny, and, concommitantly, use its political and physical resources to the maximum advantage in ameliorating the status of citizens and domestic companies.

Though decades of tedious, well-considered negotiations, the United States and its industrial trading partners were able to agree in the GATT forum to certain caveats or restrictions to the basic premise of national self-determination to address, among other things, the problems of dumping and certain export-related subsidies. While the objective standards for subsidies deemed countervailable through added duties were particularly hard won, the benefit those standards have provided in both bolstering the utility and credibility of GATT and in providing a uniform and effective import relief mechanism for U.S. and foreign companies has been commensurate with the diplomatic toil that engendered them. The proposed natural resource-pricing amendments threaten to severely undermine that benefit.

A fundamental principle of the Subsidies Code negotiated in the GATT forum and ratified by Congress by means of the Trade Agreements Act of 1979 is that a governmental assistance program which provides assistance on a uniform and industry-wide basis, such as that by which energy is provided to all industrial users in Mexico, should not be considered a countervailable subsidy. The international framework of rights and obligations imposed by the Subsidies Code, and given effect by our own Tariff Act, carefully establishes that only subsidies specifically linked to export trade or certain subsidies with a regional or industry-specific focus are actionable in import relief proceedings.

The years of negotiation, in which the United States played a leading role, which led to such specific provisions in the Subsidies Code clearly established as a matter of GATT trade policy that subsidies or other economic support programs falling outside those narrow delineations could not be fairly or reasonably characterized as countervailable practices. The proposal before the Trade Subcommittee for treating the economy-wide energy program of Mexico and similar programs seeks to expand the definition of countervailable subsidy to the point of meaninglessness, and is clearly both outside the scope of the parameters established by GATT and abhorrent to the policy behind those parameters.

2. The right of developing countries to utilize programs such as that of PEMEX is unequivocally established under GATT.—After intense scrutiny by the OECD, GATT authorities and a host of trade policymakers in the capitals of the world's primary trading countries, the right of developing countries to engage in economic practices such as that in issue here has been unequivocally established. Whether or not they are characterized as "subsidies" such practices are a vital part of economic progress in developing countries, and the U.S. has, through its GATT commitments, pledged to support them.

The GATT Countevailing Duty Code, approved by the United States under the Trade Agreements Act of 1979, expressly recognizes at Article 8(1) that "subsidies are used by governments to promote important objectives of social and economic policy." The obvious foundation of the GATT Subsidies Code is recognition that certain export-linked subsidies may disrupt international trade, and indeed, cause adverse effects in importing economies. Yet it is just as clear that the Code, as well as the General Agreements on Tariffs and Trade itself, recognizes the value and importance of certain practices in developing countries which may fall within the traditional characterization of subsidies.

As a preliminary matter, the GATT expressly recognizes that countries which can "only support low standards of living" and "are in the early stages of development" must be given certain concessions, and including latitude to engage in governmental programs desires to bolster their domestic economies despite the fact that it may have some impact on world trade.

The Subsidies Code in 1979, the Congress fully embraced the proposition that subsidies may have vitally important social and ecomomic roles in many countries, and that developing countries in particular must be permitted to use many kinds of subsidies for the purpose of promoting their social and economic development. Article II of the Code, which the Congress expressly approved through the Trade Agreements Act of 1979, specifically states that the United States and other signatories: Recognize that subsidies other than export subsidies are widely used as important instruments for the promotion of social and economic policy objectives and do not intend to restrict the right of signatories to use such subsidies to achieve these and other important policy objectives which they consider desirable.

Under Article 14 of the Code, moreover, the United States and other signatories specifically recognized that "subsidies are an integral part of economic development programs of developing countries." Accordingly, all such parties agreed that their efforts to restrict export-related subsidies through the Code were not meant to prevent developing countries "from adopting measures and policies to assist their industries, including those in the export sector." On this basis, the Code establishes that there is to be no presumption that export subsidies granted by developing countries result in adverse effects to the trade or production in other countries and such adverse impact must be specifically proven through expert analysis. The U.S. further recognized through its ratification of the Code, and specifically Articles 11 and 14, that developing country governments "may play a large role in promoting economic growth and development" in such countries and that accordingly intervention by such governments through practices which are "granted with the aim of giving an advantage" to certain domestic enterprises are fully permissible. The Code goes even so far to enumerate examples of the permitted developing country practices which, within certain limits, should be respected and supported by the industrial countries and not treated as countervailable subsidies per se. Such examples specifically include government financing of commercial enterprises, government subscription to equity capital, and government-financed provision of utility, supply distribution, and other operational or support services or facilities. The fundamental commitment of the GATT Subsidies Code to support such government programs in developing countries is reflected, moreover, in that Code's Preamble, which states as a major premises that it seeks to take "into account" the "particular trade, development and financial needs of developing countries."

In view of this existing framework, one can only surmise that the authors of the current prospects developed them in a vacuum, drafting their so-called "trade remedy" provisions as if the GATT and the GATT Subsidies Code did not exist. The domestic energy program of Mexico is a simple, across-the-board economic support program that contains no preferences, whether by region, industry sector, export sales, or otherwise. Nothing could be more clear than the fact that it is designed to promote Mexican industry generally, more specifically, to provide the type of government-financed utility service which is expressly permitted, and even encouraged, under the GATT Subsidies Code. Proponents of the provisions now before Congress would have us ignore that basic fact, and at the same time turn back the long and arduous process which over the past decades provided the framework within GATT for an international system which prevents inequities but promotes the compelling needs of our lesser developed trading partners.

C. Mexico's energy pricing policies are in full accord with international trade policy standards

Mexico's alleged "two-tiered" energy pricing policy has, of course, been fully evaluated within the applicable standards of the international trade regime, as administered by the Department of Commerce through the Tariff Act of 1930. Most recently that evaluation was conducted in the countervailing duty proceeding brought by U.S. nitrogen producers. In the final negative countervailing duty determination published June 22, 1983 and reached after an exhaustive analysis, commerce unequivocally announced that "the pricing differential for export and domestic sales of Mexican natural gas confers neither an export subsidy nor a domestic subsidy" upon the concerned Mexican industry. Although the petitioners in that case asserted, through arguments for consideration of "opportunity costs," that the export price of the gas should be considered in subsidy calculations, Commerce rejected that assertion as one which was "totally speculative" and without "basis in law or fact." The U.S. expert authorities charged with enforcing the rule of law developed in the international GATT framework have thus fully accepted the PEMEX pricing program as in accord with international countermeasure rules.

D. The "upstream" natural resource subsidy concept could not be reasonably or effectively implemented

Notwithstanding the compelling policy reasons militating against the proposed upstream subsidy standards, the U.S.-Mexico Chamber of Commerce also believes these standards suffer from practical problems which would prove insurmountable in their enforcement. The legislative proposals seek to set a duty level on imports equalling the difference between the low natural resource cost to the foreign producer ("controlled domestic price") and some second price level for that resource, variously proposed as the "export price," the "price generally available to U.S. producers," or the "fair market value." The fact that so many proposals for the second benchmark price have been offered, and the nature of differing testimony upon such a second price level, underscore the impracticality of realizing any fair means for defining that price. The variety in the specific commodities concerned, their foreign markets, the concerned buyers, the contracts for sale, and the existence of myriad actual prices make a simple objective definition of such "second level" price virtually impossible. The list of problematic questions raised by such factors is confined only by the limits of one's imagination. Which natural resources should be compared? Which natural resource prices should be compared? What quality of natural resources should be compared?

To address the first question, one need only look to the various resources utilized in the cement industries of the United States and Mexico. The U.S. cement industry recently petitioned the International Trade Administration (ITA) for protection now that oil and gas costs have been rising, reflecting a declining resource base. But circumstances inevitably change and industries adapt. Ten years ago, the U.S. cement industry used natural gas as its principal fuel. Now it uses 82 percent coal and by 1990, it will use coal for 90 percent of its energy needs because the United States has a comparative advantage in coal. The Mexican cement industry makes the best of its own comparative advantage and currently uses both natural gas and heavy fuel oil, but this also is subject to great change.

In such a case, what should be compared? The price differential between the most readily available energy source, coal, and Mexican natural gas? To what extent can one adjust for differing coal prices? Should one consider the difference between natural gas and heavy fuel oil prices available to the Mexican cement producers and the prices that would be available to U.S. producers? Who decides? When one begins to enter into such convoluted and artificial comparisons, there are no reasonable answers to such questions.

Another problem facing the Department of Commerce or any other agency administrating the countervailing duty laws would be that of identifying the actual prices used for the particular energy to be compared. Oil prices change dramatically both on a world level and in Mexico. The price of heavy fuel oil in Mexico has doubled in the last year and additional increases have averaged about 5 percent a month. Further, the price of U.S. energy varies depending on a company's location. For example, the price of oil in the Pacific Northwest of the United States is low compared to the rest of the country due to its proximity to Alaska. Is it equitable to hold Mexico to a standard U.S. energy price when a petitioning industry receives a significantly lower price itself? Attempting to calculate the difference between an exporter's home market price for gas and the average price for the same commodity in the United States can be similarly meaningless since, for example, it is a well established fact that many U.S. nitrogen producers pay two to three times more for gas than the one-third of the industry with low-cost long term contracts. How can one accommodate such disparities within any "benchmark" price framework?

If, moreover, any comparison of natural resource prices is to occur, a comparison of quality must be included. Oil in Mexico is sulphuric, corrosive and difficult to handle. It creates air quality problems which are gradually being addressed in Mexico. Mexican users are forced to make extra investments to protect their facilities by increasing the thickness of their pipes, installing special coatings inprocess equipment, and sustaining higher maintenance costs and longer downtime periods for their machinery and equipment. It is true that Mexico has certain comparative advantages over the U.S. in some energy resources, but these advantages are far from absolute; those advantages are not, moreover, likely to remain static over the course of coming years.

Such a review of the administrative inadequacies of the instant proposals could become almost endless due to the many variations in products, price, location, use government would be plunged into a quagmire of changing prices, changing resources and changing qualities. It would be hopeless to expect U.S. officials to come up with any meaningful rates within the short period of an investigation, and, in any event, the conditions will almost always have changed before a determination is issued.

E. The proposed countermeasures will have severe adverse effect on U.S. agricultural and other interests

Notwithstanding the compelling international trade policy reasons militating against the current proposals, on the basis of the adverse domestic impact alone they should be rejected by this Subcommittee. That impact only begins with the inevitable large cost increases that would be suffered by both U.S. farmers and construction contractors, who are primary users of the products, which will be a primary target of the proposed countermeasures. Such industries may be viewed as perhaps least able of any U.S. industries to afford such increased costs, and least able to maintain international competitiveness under such conditions. Ultimately, moreover, due to the inevitable loss of Mexican supplies which would be caused by these proposals, U.S. industrial energy users would find themselves bidding against U.S. residential consumers for energy.

These proposals will, however, also affect a much broader cross-section of our economy in a manner that, although more subtle, will be even more pernicious. Roughly 40 percent of our exports are shipped to developing countries. This market has grown rapidly in recent years and is expected to continue in the future. These countries need U.S. dollars to purchase our exports. They obtain dollars by exporting goods to the U.S. which are often produced from their natural resources. Cement is a prime example. If these exports are discontinued, three highly undesirable events will occur: (1) the developing countries will not have the dollars to purchase our exports; (2) the actual development of these countries will be slowed, resulting in a potential loss of future U.S. exports and an increase in the political instability of these nations; and (3) the developing countries will be forced to default on their collectively huge debt to U.S. banks, significantly decreasing the money supply and increasing the interest rates to our domestic industries.

An impact more difficult to quantify but just as certain to transpire is that resulting from retaliation by countries affected by such unilaterally-imposed countermeasures outside the GATT framework. The efforts made by the U.S. at the Williamsburg Summit and in Geneva to forestall "creeping protectionism" by our trading partners would lose all credibility were these proposals to be enacted. The U.S moreover, is in a particularly vulnerable position with its own energy program, which has also been attacked as unfairly "two-tiered" by our Western allies. After raising barriers to imported steel, renewing textile restrictions, and administering sweeping restrictions in automobile trading, our government has placed itself in a position that almost guarantees reciprocal protectionism if it enacts further protectionist measures.

CONCLUSION

In summary, the proponents of the upstream national resource subsidy proposals before this Subcommittee have embarked upon a dangerous course that threatens to gravely undermine not only U.S. relations with Mexico and other developing countries but also the U.S. effort over the past 35 years to establish a rule of law and reason in international trade. Current U.S. import relief law provides a broad framework for remedial measures under that rule, and this attempt to invoke countermeasures in a manner which extends far beyond that rule not only flouts the system this country has worked so hard to develop but also invites retaliation by our trading partners.

The message sent by these proposals should be loud and clear. It should reaffirm what was said in Geneva: what matters in the international trade framework is the rule of fairness and not the bowing to special interest groups. The United States-Mexico Chamber of Commerce strongly urges this subcommittee to reject the "upstream" natural resource subsidy proposals now before it.

Thank you.

O