# ANNEX C

REBUTTAL SUBMISSIONS OF PARTIES

# ANNEX C-1

## EXECUTIVE SUMMARY OF THE SECOND WRITTEN SUBMISSION BY THE REPUBLIC OF KOREA

19 July 2004

## I. SUBSIDY ISSUES

### A. The Scope Of “Entrusts Or Directs”

#### 1. The meaning of “entrusts or directs” imposes legal limits

1. The United States acknowledges but then ignores the legal limitations imposed by Article 1.1(a)(i)(iv). In particular, the United States has ignored the core meaning of both of these key terms.

##### (a) Text

2. Both the word “entrusts” and the word “directs” convey the basic meaning of carrying out some specific action. The United States claims that guidance or suggestions alone would be sufficient to establish “entrusts or directs”. Yet “directs” has a much stronger meaning, and conveys the idea of ordering the private party to do something. Also, in light of the French and Spanish texts, the most appropriate interpretation of the English word “directs” must be the meaning of ordering [illegible]

### 2. *US-Export Restraints*

6. The United States tries to downplay the relevance of *US-Export Restraints*, by arguing that panel decision considered a different factual context. But this effort to distinguish *Export Restraints* fails on two levels. First, the panel in that case was clearly offering its own reading of the specific text at issue here. Second, that panel also wisely explained the problems with an overbroad reading of "entrusts or directs". In particular, the panel distinguished carefully between government interventions and actions that by their nature rise to the level of "entrusts or directs".

### C. The DOC's Other General "Evidence"

#### 1. Gene ral problems with the US approach

11. In general, the United States cites evidence regardless of the time period and regardless of the connection to the Hynix restructuring. The United States also makes numerous factual misstatements.

12. In addition, there are several problems with the evidence of an alleged policy to save Hynix. The core US argument in this regard focuses on the Economic Ministers meetings in late 2000. But this discussion illustrates the shortcomings in the US approach. The United States also argues that Hynix was somehow exempt from its review of financially insolvent companies, citing a single newspaper article as evidence. Yet the FSS/FSC never exercised any pressure to exempt any companies from the list of companies to be liq uidated.

#### 2. Alleged control over creditors

##### (a) Signalling & Ownership

13. The United States repeatedly invokes the idea of "signalling". The problem for the US theory is that such evidence is legally irrelevant to the issue of entrusts or directs. The United States also invokes GOK ownership in the banks, but in so ding, ignores the various procedural safeguards imposed by the GOK.

##### (b) Kookmin Prospectus

14. The United States makes much of the Kookmin prospectus, but this approach to the Kookmin prospectus overlooks several important pieces of evidence. Among others, the possibility of GOK influence is belied by the actual actions of Kookmin in the October restructuring.
Prime Minister's Decree & Public Funds Oversight Act/MOUs

##### (c) Prime Minister's Decree & Public Funds Oversight Act/MOUs

15. The United States mischaracterizes the Prime Minister's Decree No. 408. As Korea already explained, the United States completely ignores Article 1 of the Decree. Instead the United States mischaracterizes other parts of the Decree. The United States ALSO cites to the MOUs as somehow providing a mechanism of control. Unlike the US assertion, however, the purpose of the MOUs is to ensure that the bank can recover quickly Pro Twd3080 TKr4r(b)D s0 Tc7 Tw (h(however8 Tc -0.pga23
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### 4. DOC improperly rejected Citibank as a suitable benchmark

#### (a) Rejecting Citibank is inconsistent with Article 14(b)

23. The DOC's rationale for rejecting Citibank as a suitable benchmark was based on a "circumspect finding" of "unusual aspects" in connection with Citibank's loans to Hynix. Yet in light of what the Appellate Body has found in *US - Lumber,* this rationale does not meet the standard set forth in Article 14(b).

#### (b) The DOC's rationale for rejecting Citibank is not supported by positive evidence

24. The United States continues to insist on viewing Citibank's loans in the context of total financing. Such approach, however, underscores the danger of allowing an investigating authority to utilize whatever methodology of its choice. Also, when one considers Citibank's participation in the transactions as they occurred, it is very much comparable to the commitments of other Hynix creditors in those transactions.

### 5. Korean default rates

25. Even assuming DOC was somehow correct in its approach to creditor benchmarks, there was no basis to ignore Korean default rates in calculating its "uncreditworthy" interest rate benchmark. At the very least, the DOC was obliged to explain why the US data related or referred to prevailing

### B. US Interpretation of the Causation Standard

30. The US reading of Article 15.5 of the SCM Agreement would render the causation requirement of that provision largely meaningless. In its First Submission, the United States resists what is now well-established principle that Article 15.5 requires authorities to disentangle causes, including subject imports, so as not to attribute injury to subject imports caused by other factors.

#### 1. Interpretation of "causal relationship"

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47 The ITC defence of its averaging methodology actually admits the defects in the rationale. Specifically, the United States noted that transaction-specific data "would be more suitable", admitting the reality that more detail is better than less detail in trying to understand pricing dynamics. But because transaction specific data sometimes is onerous to collect, the United States then swings to the opposite extreme, and largely ignores the disaggregated data *that it actually did collect in this case*.

### (b) Price effects of subject imports

48. The United States asserts that Hynix undersold more often than any other source, a conclusion that it reaches only by distorting the presentation. It disaggregates the other suppliers into domestic and import sources, thus making them appear smaller. The United States also ignores the fact that during the investigation period, Hynix's US manufacturing facility shut down. Finally, the United States does not put the combined volume of the other suppliers into proper context. Even if nves58.5 06T conteu t conteu t Tj 109.75 Td

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demand growth rate had dropped by nearly two-thirds. Also, Micron and Infineon explicitly acknowledged a direct correlation between the decline in the demand growth rate and harm to the domestic industry.

#### 3. Increased capacity of other suppliers

55. What the evidence before the ITC demonstrated was that DRAM manufacturers other than Hynix were dramatically increasing their capacity. The ITC completely ignored this evidence. To date, neither the ITC nor the United States have adequately explained, or really even considered, the role of capacity expansion by producers other than Hynix on the performance of the domestic industry. Moreover, the data on relative capacity changes in this case strongly corroborated Hynix's argument that other suppliers were offering the lowest prices and had a much more substantial effect on price levels.

#### 4. Injurious effects of Micron's technological difficulties

56. In its First Submission, Korea includes 16 paragraphs that provide evidence and argumentation concerning the significance of Micron's admitted technological difficulties on its financial performance. In response, the ITC merely provides a single <u>footnote</u> of just <u>three</u> sentences. As importantly, the US never recognizes that if Micron experiences difficulties, it has a substantial impact on the performance data for the industry as a whole.

### E. The Condition of the Domestic Industry

57. In its discussion of the condition of the US DRAM industry, the United States largely repeats the recitation of facts that appeared in the ITC determination in the first instance. The United States takes apparent pride in its "wealth of data". But collecting data does not mean the data has been

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### C. The Countervailing Duty Order is Properly Before This Panel

61. The United States argues that Korea did not provide any "indication" of the legal basis for its challenge to the countervailing duty order. Yet the two consultation requests of the GOK provide a fairly detailed explanation of the legal defects with the DOC and ITC determinations. Since the US countervailing duty order rests on the legal and factual foundations of these two agency findings, Korea was in fact providing a more than sufficient "indication" of the legal basis for its claim.

### D. The Panel May Consider Any Evidence It Deems Appropriate

62. At the first meeting with the Panel the United States raised the argument that the Panel may only consider information submitted to the administering authorities. Korea believes this argument is wrong as a matter of law. The only relevant textual obligation on panels under the SCM Agreement is found in Article 11 of the DSU. Moreover, this more flexible approach makes sense. If the authorities have not asked the right questions, or did not clarify certain information, then those failures might well be part of the "objective assessment" that the panel must provide.

did influence its lending decisions. Moreover, Kookmin's financial statements suggested that the statements in its prospectus related to Hynix. Kookmin's 2001 Annual Report listed Hynix as its single largest financially troubled borrower.

7. With respect to the CRPA, the GOK enacted the CRPA precisely at the time when Hynix and other Hyundai Group companies were on the brink of bankruptcy and required significant financial assistance to avoid financial failure. Citibank officials characterized the CRPA as a way for the larger creditors to force their decisions on smaller creditors. Independent analysts, such as Standard and Poor's, noted that the CRPA provided the GOK with "a powerful voice in lending decisions", and concluded that the GOK could utilize its powers to "force some financial institutions to make new loans against their will" and "strip[] the financial services companies of their independence in lending decisions". Thus, while the CRPA may have been modelled in some respects on the so-called "London Approach", the GOK's version was government-driven, with the GOK playing a direct role in working out debts with financial institutions owned and controlled by the GOK.

8. The structure of the CRPA enabled a handful of banks – the "Creditors' Council" – to dominate the restructuring process, to establish the terms and details of the agreement, and to dictate the results to every other creditor, and this is what happened in the Hynix October restructuring. Citibank confirmed the effectiveness of this voting structure, stating that "creditor banks holding 75 per cent of Hynix' debt can impose their decisions on everyone else ... [and that, while] foreign creditors wanted more freedom to manoeuvreci4 Tj -36 Tependentj 3adn222 debtlon

12. Another of the GOK's actions aimed at effectuating its policy to ensure the survival of Hynix was the GOK's pressure on credit rating agencies. Agencies cancelled plans to downgrade or were forced to upgrade credit ratings. Lower credit ratings would have made it more difficult for the GOK to continue its Hynix bailout programme, which was already the subject of intense criticism.

13. Governments may have political reasons for wanting to obscure their role in providing assistance to a particular company or industry. Thus, cases involving indirect subsidies can present particular challenges for an investigating authority attempting to gather facts and figure out what really happened. If Article 1.1(a)(1)(iv) is to have any meaning, it is essential to recognize the importance of examining, on a case-by-case basis, all of the evidence, including primary, secondary, and circumstantial evidence, surrounding possible government entrustment or direction.

14. In the case of the Hynix bailout, the reasonableness of the DOC's conclusion that the GOK entrusted or directed Hynix's creditors is not even a close call. The DOC considered a wide range of evidence. With respect to secondary sources, prior panel reports provide support for the DOC's reliance on secondary sources and the drawing of reasonable inferences based on the record evidence. In the DRAMs investigation at issue in this dispute, the secondary sources in the record have been shown to be credible and are often corroborated by other reports or documents. Moreover, the Appellate Body has recognized the permissibility of relying on reasonable inferences. Thus, it is not the *type* of evidence that matters. Rather, the issue is whether the domestic authority examined all the pertinent facts and provided an adequate explanation as to how the facts support its determination. The DOC did so in the DRAMs investigation.

15. **<u>Benefit</u>:** In determining the existence of a benefit, the issue is the position of the recipient "but for" or "absent" the government's financial contribution. Only by comparison to a market undistorted by the government's financial contribution is it possible to determine whether the recipient is better off than it otherwise would have been absent the financial contribution.

16. Article 14 does not redefine the concept of benefit in Article 1.1(b). Article 14 merely provides guidelines that must be followed in establishing "methods" for applying that concept to particular types of financial contributions. Therefore, each guideline in Article 14, including the guideline contained in Article 14(b), must be interpreted in a manner that is consistent with the meaning of the term "benefit" as used in Article 1.1(b) of the SCM Agreement.

17. With respect to Citibank, consistent with Article 14 of the SCM Agreement, the DOC examined the pertinent facts surrounding the loans and equity investments from Citibank and provided an explanation as to why they did not qualify as appropriate benchmarks. The reasons why the DOC rejected Citibank as a suitable benchmark are discussed extensively in the paragraphs 197-204 of the US first written submission.

18. With respect to the DOC's use of historical cumulative default rates published by Moody's Investor Service to calculate the uncreditworthy benchmark rate used to measure the benefit to Hynix, nothing in Article 14 of the SCM requires that the DOC use Korean default rates to measure loans benefits. In fact, the DOC examined but rejected the Korean default rates provided by Hynix. First, there was no information provided with the rates offered by Hynix that would have allowed the DOC to ascertain how they were calculated. Second, there was nothing indicating that the historical rates were cumulative average rates, as required under the DOC's regulations. Only cumulative rates provide the probability of default over the full term of the loan, as opposed to a single year. Third, the default information submitted by Hynix was unreliable on its face, because the data suggested that the default rate for the lowest rated debt was lower than the default rate for the highest rated debt. This inverse relationship made no sense. Accordingly, the DOC reasonable declined to rely on the rates offered by Hynix, because they lacked sufficient information and appeared unreliable on their face.

26. **Price Effects:** The ITC engaged in one of the most data-intensive, complex pricing analyses it has ever undertaken. The pricing data the ITC collected were clearly representative, accounting, by value, for approximately 45.9 per cent of domestic producers' and 36.9 per cent of subject imports' US shipments in 2002. Based on a weighted-average comparison of the price of domestic shipments with the weighted average price of subsidized subject imports for each month of that time period, the ITC found significant price undercutting by subsidized subject imports.

27. The level of detail of pricing data obtained by the ITC provided unassailably accurate head-to-head price comparisons. The level of accuracy and objectivity of examination permitted by the monthly series of weighted-average price comparisons by product and by channel of distribution was remarkable. These data permitted the ITC to determine in those monthly periods for which price comparisons were available whether the subsidized subject imports were underselling or overselling the domestic like product and by what margins. Based on this extensive data, the ITC ascertained that for the majority of possible comparisons, subsidized subject imports undercut the domestic like product at high margins (often over 20 per cent), and at increasing frequencies (from 51 per cent of possible comparisons in 2000 to 56 per cent in 2001 and 70 per cent in 2002). The ITC identified significant price undercutting to each of the three main channels of distribution (PC OEMs (*i.e.*, original computer equipment manufacturers), other OEMs, and non-OEMs). The ITC also found that undercutting was consistent and substantial for particular high-revenue products to particular channels of distribution at specific points during the period of investigation. The ITC went well beyond the approach found to be WTO-consistent by the panel in *EC – Tube*.

28. The ITC also went well beyond the requirements of the SCM Agreement by collecting and evaluating pricing data on non-subject imports. Korea's argument in its opening statement that the ITC "ignored the prices of non-subject imports" in its pricing analysis is simply wrong.

29. The pricing data show that the underselling frequency by non-subject imports was lower than, and increased less than, the underselling frequency of subsidized subject imports between 2000 and 2002. In particular, while subject imports were increasing their underselling frequency between 2000 and 2001 from 51 per cent of all observations to 56 per cent of all observations, the frequency of underselling by non-cent of agraascerta15 5 TD as g analysi[illegible]

factual data on undercutting was probative. These included the high degree of substitutability between subject imports and the domestic DRAM products, the overlapping customers and channels of distribution to which subject imports and the domestic DRAM products were sold, the inelasticity of demand, and the importance of price in this particular industry.

33. A finding of undercutting, let alone significant undercutting, is not a prerequisite to an affirmative injury determination. Article 15.2 of the SCM Agreement specifically provides that "[n]o one or several of these factors can necessarily give decisive guidance". Nevertheless, it is clear that, under the analysis the ITC conducted in this investigation, there was *significant* undercutting by subsidized subject imports.

34. The ITC also found that subsidized subject imports depressed prices to a significant degree. Korea does not challenge the ITC's finding that there was significant price depression by subsidized

imports into its analysis of the volume, price effects and impact of subject imports. While this approach is not required by the SCM Agreement, it is certainly consistent with the Agreement. Korea fails to show otherwise.

39. Korea's arguments reveal that it believes that in investigations like the DRAMs investigation, where there are several factors that may be injuring the domestic industry, an investigating authority is precluded from making an affirmative material injury determination. Korea's argument has no basis in the provisions of the SCM Agreement. Appellate Body reports also lend the argument no support.

40. The ITC also examined other known factors to ensure that it did not attribute injury from those factors to the subsidized subject imports. In so doing, the ITC properly separated and distinguished other known factors from the subsidized subject imports by providing a satisfactory explanation of the nature and extent of the injurious effects of the other known factors, as distinguished from the injurious effects of the subsidized subject imports. This is all that is required, even in the context of the Safeguards Agreement.

41. For example, with respect to the business cycle, the ITC found that because growth in demand for DRAM products has been continuous, but supply increases are sporadic, supply and demand in this industry tend to be chronically out of equilibrium, giving the market its characteristic "boom" and "bust" business cycle. The ITC also determined that largely because of the perpetual improvements in production efficiencies experienced by this industry, prices are usually declining. At the same time, the ITC determined that the business cycle (and other factors affecting prices) simply did not explain the unprecedented severity of the price declines that occurred from 2000 to 2001 and that persisted through 2002. Nor could it explain the increasing frequency of underselling by subsidized subject imports during the period of investigation.

42. The ITC's examination of other known factors is identical to the methodology upheld by the panels in *EC – Tube* and *Egypt – Rebar*. The panel in *Egypt – Rebar* did not require the "non-attribution" findings of the investigating authority to be based on an econometric model or some sophisticated quantification exercise. All that the panel in *Egypt – Rebar* required was that the "non-attribution" findings be based on a meaningful explanation as to why the effects of the subsidized imports did not "overlap" with (that is, were notionally distinct from) those of another factor causing injury at the same time. In the DRAMs investigation, the ITC found that the *subsidized imports had price effects that significantly exceeded those of non-subject imports*, and that other factors – such as the operation of the business cycle (including by virtue of capacity/supply increases); slowing in the growth of demand; and the product life cycle – could not explain the unprecedented price declines experienced during the period of investigation. Therefore, it is clear that subsidized imports had their own, independent, injurious effects.

43. As in *EC – Tube*, the ITC found that effects of one factor (capacity expansions) were subsumed within the effects of another factor (the operation of the business cycle), and determined that the effects of the latter factor could not explain the totality of the injury observed (cumulative price declines that ranged as high as 90 per cent, well in excess of the "usual" ranges). These findings supported the ITC's conclusion about the causal nexus between the subsidized subject imports and the injury to the domestic industry.

**E. Korea does not Dispute the ITC's Treatment of Certain Data as Confidential and Offers no Basis for the Panel to Request Confidential D**