



US Steel Safeguard Dispute

Forged Protection brought to Light

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In a highly competitive world steel market, countries sustain their own steel industry through extensive use of subsidies and trade barriers. Often, they are even forced to tolerate private cartels. The steel market is, therefore, probably the most deeply distorted industrial market in the world economy. Indeed, financial health of the steel industry has suffered from inefficient production, as companies and governments support high-cost local capacity and market intervention in the form of quotas, subsidies and tariffs.

Safeguard measures applied by the US on imports of certain steel products were inconsistent with the obligations of Agreement on Safeguards, General Agreement on Tariffs and Trade (GATT) 1994 and Article XVI of World Trade Organisation (WTO) Agreements. The case against tariffs was brought by the European Union (EU), which charged that the US was illegally protecting its domestic steel industry. The tariffs in steel market mainly hit steel makers in the EU, Japan, Korea, Norway, Switzerland, New Zealand and Brazil. Appellate Body (AB) in upheld the Panel report and confirmed that the US had failed to meet the basic pre-requisite conditions required before any safeguard action could be implemented regarding unforeseen developments, increased imports and exclusion of imports from certain sources. This paper, discusses the various aspects of the case, including the impact of this ruling.

Facts of the Case

In June 2001, the United States International Trade Commission (USITC) initiated a safeguard investigation under section 201 of the Trade Act 1974 to determine whether the import of steel products was causing injury to domestic industry producing similar or directly competitive products. USITC made affirmative determinations of serious injury to the domestic industry on account of imports of various steel products.

Based on USITC determination, the President of the US imposed definitive safeguard measures on imports of certain steel products in March 2002. The President imposed tariffs of nearly 30 percent on the import of steel products from Europe, Asia and South America, the biggest government action to protect domestic industry. On June 3, 2002, a WTO dispute settlement Panel was established at the request of the European Communities to examine the consistency of the US safeguard measures with WTO rules. Complaints on the same issue by Japan, Korea, China, Norway, Switzerland, New Zealand and Brazil were subsequently submitted to the same Panel.

The Agreement on Safeguards and Article XIX of GATT 1994 provide that a WTO member may apply safeguard measures only if, following an investigation by competent authorities, it determines that imports have increased, that the increase was a result of unforeseen developments, and that the increased imports have caused, or threatened

to cause, its domestic industry to suffer serious injury. The Agreement further provides that the competent authorities must issue a 'report setting forth their findings and reasoned conclusions reached on all pertinent issues of fact and law'.

Arguments and Counter Arguments

The US requested that the AB reverse the Panel's findings that the USITC failed to provide a reasoned and adequate explanation demonstrating that 'unforeseen developments had resulted in increased imports causing serious injury to the relevant domestic industry.'

The US argued that 'the Panel based many of its findings against the US on its conclusions that the USITC report failed to provide a 'reasoned and adequate explanation' of certain findings. The US further argued that a failure to explain a finding does not automatically prove that the USITC had not performed the analysis necessary to make the finding.

Brazil submitted that the articulation by the Panel of the applicable standard of review is consistent with the Agreement on Safeguards and previous findings of the AB. Referring to the phrase 'reasoned and adequate explanation', Brazil noted that although 'adequate' and 'explanation', are not explicitly found in the text of the Agreement on Safeguards, both terms 'are easily discerned' from what is in the Agreement, and particularly the language found in Article 3.1 and Article 4.2(c) of the Agreement on

Safeguards (that is, ‘reasoned conclusions’ and ‘detailed analysis’ and ‘demonstration of the relevance of factors’). Brazil argued that the US not agreeing with the Panel’s rationale does not imply that the Panel has not rendered a right verdict with regard to Article 12.7 of the Agreement on Safeguards. China requested the AB to reject the US’ appeal of the Panel’s conclusions concerning unforeseen developments. China argued that the Panel applied the correct standard in requiring that a report must contain a coherent and logical explanation with respect to unforeseen developments. The European Communities recalled that, as the AB found in the *US-Lamb* case, the existence of unforeseen developments is a ‘pertinent issue of fact and law’ within the meaning of Article 3.1 of the Agreement on Safeguards and, therefore, the ‘report of the competent authorities, ... must contain a finding or reasoned conclusion on unforeseen developments’.

Appellate Body’s Verdict

The AB’s ruling on November 10, 2004 largely upheld the Panel’s conclusions, specifically its focus on the inadequacy of the US explanation on how the facts supported the conclusion that each of the elements of a safeguard case had been met. It is noteworthy that the WTO violation resulted from the inadequacy of explanation and not from a fault in the US law. The AB emphasised throughout its report that safeguard measures were considered extraordinary measures and that consequently WTO members had an obligation to clearly set forth the rationale for their determinations.

On the question of increased imports, the AB ruled that the USITC failed to provide a reasoned and adequate explanation on how the facts supported its determination that the increase in imports had been recent enough,

sudden enough, sharp enough and significant enough to cause serious injury.

On the issue of ‘unforeseen developments’, the AB concluded that the USITC report was wanting in reasoning. The USITC had found that the Asian and Russian financial crisis, together with the strong US dollar and economy, were the cause of the increased imports and that these economic developments were ‘unforeseen’. The AB did not question the existence of those developments or the claim that they were unforeseen and neither did it question that the developments might have caused the import surge. Rather, it ruled that USITC had failed to provide a logical explanation of how such causation actually occurred.

The AB declined to rule on the general question of whether the USITC had failed to demonstrate a causal link between increased imports and serious injury, viewing such a decision as unnecessary in light of the other violations.

But the AB found that, in the absence of an explicit statement of reasoning related to each safeguard action, a dispute Panel is justified in determining that the standard for decisions on safeguards has not been met. The Panel is not required, said the AB, to review the evidence *de novo* to determine whether it provided the basis for a reasoned and adequate conclusion. The adequate reasoning must be explicit in the safeguards decision.

The AB upheld the principal finding of the dispute panel: that the US authorities did not justify their decision to impose temporary ‘emergency’ tariff increases (safeguards) on imported steel. In brief, they failed to show that the emergency described in their decision actually led to an unforeseen increase in steel imports that was harming the US steel industry.

Box 1: Legal Remedies at WTO: Too Little Too Late

First, no damages are awarded for harm caused in the past. In other words, the US did not have to compensate anyone for the 21 month lifespan of the WTO-inconsistent steel safeguard. This loophole offers a clear incentive for hit-and-run practices where countries enact protectionism, knowing that it is illegal, but also realising that they can get away with it – ‘for free’ – for at least as long as it takes to complete dispute settlement proceedings.

Second, once the WTO has made its final ruling and an on average one-year time to implement such ruling lapses (during none of which any compensation is owed), trade sanctions can, indeed, be imposed. In safeguard disputes, such as the steel case, retaliation is permitted even *before* that, namely directly after the WTO has issued its final ruling (another factor that may have prompted earlier implementation in that case). Although a threat of retaliation by the EU may be both real and harmful even for a country like the US, but if and when the threat comes from, for example, Egypt or Thailand, it may not even reach the ears of the US President. Put differently, trade sanctions – in essence the only legal remedy available at the WTO – may (sometimes) work for powerful complainants, they are unlikely to work for smaller players. On the contrary, rather than putting pressure on the violating country, when

a small player retaliates it is more likely to harm its own economy (higher input and consumer prices) as well as its own political interests (e.g the risk of being cut-off from foreign assistance).

Third, in addition to the absence of retroactive remedies and the often unpalatable nature of trade sanctions, the *amount* of retaliation that the WTO can authorise is capped at the equivalent of the trade kept out by the original violation, in this case, the continued imposition of the WTO illegal safeguard. This is nothing more than a simple tit-for-tat or zero-sum game where, in principle, no more pressure is put on the violating country (by the trade sanction) than on the victim (by the original violation).

Given these deficiencies, one may ask why WTO members still comply with 90 percent of WTO rulings and, in particular, developing countries have rarely faced the problem of non-implementation. The most likely answer is that it is not the *legal* remedies, nor the *economic* pressure exerted by trade sanctions that induce countries to behave. Rather, it is the *political* pressure of peer review, example setting and shunning *internationally*, at WTO meetings, and the *domestic* political pressure, from both sectors harmed by the original violation (steel consumers).

Box 2: Why Resolving Steel Case was Easy

Although a trade war over steel has now been averted, a rather long list of non-implemented WTO rulings remains, most of them decisions against the US (Foreign Sales Corporations, Anti-dumping Act of 1916, Byrd Amendment, Canada/Brazil Aircraft disputes and the EU hormone-beef ban). Conforming to WTO rules in the steel case was, indeed, relatively easy.

- First, the US President could do it on his own. In contrast to, for example, the ongoing Foreign Sales Corporations dispute, there was no need for Congressional approval.
- Second, the violation of WTO rules in the steel case was rather obvious. No one expected the US to win. The protection was not even sold as a response to unfair or dumped steel imports, rather it was labelled as a 'safeguard', that is, in the words of the AB, import restrictions on perfectly 'fair trade' from other WTO members. If, in these circumstances, the US had refused to comply, it would have lost a tremendous amount of credibility on any next occasion where it was insisting on others to comply with free trade principles.
- Third, and most importantly, by the time the protection on steel was lifted, the safeguard had met most of its objectives, both political and economic. By enacting the safeguard, the US administration gained the much-needed support from the steel lobby in matters, such as fast-track authority from Congress to conclude other trade agreements. Moreover, by keeping the WTO-inconsistent safeguard in place for 21 months, the US steel industry was given a time-out from import competition without the US having to 'pay for it' at the WTO. As President Bush openly stated, 'these safeguard measures have now achieved their purpose ... it is time to lift them'.

In short, the Panel on July 11, 2003 ruled in favour of the co-complainants that the US steel safeguards are inconsistent with WTO rules because:

- the US failed to demonstrate that the alleged increased imports were the result of unforeseen developments;
- for most products, imports have not increased;
- the US did not properly establish the causal link between the alleged increased imports and the purported serious injury faced by the US steel industry; and
- the US excluded imports from Canada, Mexico, Israel and Jordan from the measures in violation of WTO obligations.

Ramifications of the Ruling

It is debatable whether the US steel industry has benefited much from the measures, as the main purpose was to allow north American producers to fill the gaps left by the exclusion of traditional suppliers, such as the EU. At the same time, US consumers have had to pay more for specific types of steel that are only available in sufficient quantities from those traditional sources. The WTO said that the US policy, which increases the cost of imported steel by as much as 30 percent, could not be justified by the putative reason of giving the US steel industry a three-year respite from international competition, perhaps noting that the decline in the US steel industry is a decade long phenomenon. The tariffs also hurt US steel users, such as homebuilders and auto companies that buy steel. The US policy has been riddled with so-called exemptions to manufacturers which are designed to minimise its effect, but which were not enough to make it legal.

The important consideration for steel consumers is not whether prices are higher or lower but whether prices are higher or lower in their own market than in other markets around the world. When prices are lower in other global markets, steel consuming manufacturers are

at a serious competitive disadvantage. They lose work and jobs to non-US competitors.

Many of the steel products covered by the US safeguard action are already subject to anti-dumping (AD) and/or countervailing duty (CVD) measures. A total of 21 AD orders against EU exporters are pending on products already covered by the safeguard measures. The termination of safeguard actions does not have any impact on the outstanding AD and CVD orders.

The US safeguard measures had a strong impact worldwide and triggered a dangerous 'domino effect'. Several other WTO members (including the EU in September 2002) decided to impose similar measures to avoid possible trade diversion of steel products otherwise directed to the US. Removing the US measures would allow lifting these other national barriers and restoring exporters' confidence in international steel trade. The EU has always declared that it would remove 'its' safeguards as soon as the US would remove 'theirs' given that the EU safeguards were only taken in response to the US measures.

An improved international climate would also enhance the chances of success of the international Organisation for Economic Cooperation and Development (OECD) talks on strict steel subsidy disciplines worldwide and on steel capacity reductions. By lifting the steel safeguards and thus eliminating the biggest distorting of world steel trade, the US would certainly send a strong message to the other 40 members of the OECD steel talks, to further demonstrate a strong commitment to reach an international Steel Subsidies Agreement (SSA) aimed at reducing trade-distorting steel subsidies, the main responsible for global excess steel capacity.

The US lost its credibility as a champion of free trade. It has widened the chasm between the EU and the US. More painfully, it created an unbridgeable gap between the developing and developed countries.

Impact on Other Countries

The Australian steel industry has faced difficult challenges for long. After the US imposed tariffs on steel imports in March 2002, the crisis confronting the industry threatened the closure of its most important export market. But in the wake of the tariff increase, Australia successfully negotiated exemptions for 85 percent of its steel exports to the US. Around 7 percent of exports did not qualify for exemption because exports of cold-rolled steel to the US market were at dumped prices.

Following the US decision, a succession of countermeasures by steel producing countries threatened a return to trade protectionism. The reaction to the US tariffs was immediate and draconian. The large steel producing countries, the EU and China introduced their own steel tariffs, which have since led to higher steel prices in those markets. In Australia, tariffs or anti-dumping duties were imposed on imports of structural steel, raising prices and expanding domestic sales. As a result of the duty increase, One Steel has increased sales volume and doubled its half-year net profit for the period ended December 2002.

The farm and steel subsidies provoked anger among big Latin American countries-Argentina and Brazil- and stalled the negotiations on the Free Trade Agreement of the Americas (FTAA). For developing countries like India and Brazil, the steel sector is pivotal to growth. If it slumps due to the vicissitudes of international trade, these countries would be seriously hurt.

Conclusion

Safeguard measures can be used in moderation and the in prevention of abuse – although it is difficult, the Safeguards Agreement must contribute to maintaining this balance of moderation and its prevention. The current system, however, clearly lacks this balance because safeguard measures themselves are very difficult to handle

Box 3: Impact of Tariffs in the US

The US Steel corporations and the United Steel workers Union wanted the tariffs in place to avoid further disruption in the industry. Conversely, a coalition of steel consuming industries urged to discontinue the tariffs, which had hurt them and resulted in loss of jobs of thousands and pointed out that EU retaliation will make things worse. The tariffs were allegedly meant to protect steelworkers. But in the US, steel users employ roughly 40 times more people than do steel producers. Thus, according to estimates by the Institute for International Economics, between 45,000 and 75,000 jobs were lost because higher steel prices made the US steel using industries less competitive. Steel prices soared after the tariffs were put in place and raised the cost for user industries. Some 35 steel mills had declared bankruptcy till March 2002. The US Steel Industry could not face competition from newer mills within the US or producers from Asia, Latin America and the Confederation of Indian States (CIS), all of which had the advantages of newer technologies, lower labour costs and no legacy costs, such as pension and medicare.

Source: S. Sethuraman, *Business Line*, 21.11.03

and rebalancing still remains vulnerable. The US steel case brought these issues into sharp relief again and prompted member nations to reconsider what safeguard measures should be under the WTO regime.

However, the reality is that revision of the Safeguards Agreement is not included in the Doha Development Agenda (DDA). Even if it had been included, it is not hard to imagine that negotiations would have fallen into a quagmire as a result of lengthy debates on technical issues, just as in the ongoing negotiations to clarify and improve the Anti-dumping Agreement. Under such circumstances, there is probably no other choice for the time being but for member nations to exercise prudence and refrain from the political abuse of safeguard measures so as not to burden the WTO system.

In addition, the WTO Dispute mechanism was found to be the major problem in this case and not the safeguard agreement. This can be stated, as there was lack of enforcement of judgement pronounced by WTO Dispute mechanism to the US. The mechanism is partial towards the developed countries in its implementation.

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