



**American
Iron and Steel
Institute**



April 27, 2006

Hon. Marilyn R. Abbott
Secretary to the Commission
United States International Trade Commission
500 E Street, SW
Washington, DC. 20436

RE: U.S.-Republic of Korea Free Trade Agreement: Written Comments Concerning the Probable Economic Effect of Providing Duty-Free Treatment for Imports

Dear Ms. Abbott:

In response to a request from the United States International Trade Commission (ITC),¹ the American Iron and Steel Institute (AISI), The Steel Manufacturers Association (SMA), and the Specialty Steel Industry of North America (SSINA), on behalf of its U.S. member companies², hereby submits written comments to the ITC, and advice on, the U.S.-Republic of Korea (ROK) Free Trade Agreement (FTA), and the Probable Economic Effect of Providing Duty-Free Treatment for Imports.

The stated objective of this proposed FTA is to remove tariffs and expand trade. With regard to tariffs and bilateral U.S.-ROK steel trade, both countries committed to go to zero tariffs on steel in the Uruguay Round and both are already at zero (normal) duties on steel imports from each other and the world. Thus, from a steel standpoint, when we look at the potential gains or losses from a possible FTA with Korea, we find it necessary to go beyond the issue of steel and steel tariffs, and to look closely at other factors, in particular: (1) non-tariff barriers (NTBs) and "indirect" steel trade; (2) "new" issues such as exchange rates and border-adjustable taxes; and (3) the broader trade context.

I. History of Unfair Trade in Steel

¹ See United States International Trade Commission, "U.S.-Republic of Korea Free Trade Agreement: Advice Concerning the Probable Economic Effect of Providing Duty-Free Treatment for Imports," Invoice numbers TA-131-032 and TA-2104-021 (February 22, 2006).

² Our members, together, account for nearly all of the carbon and specialty steel mill products produced annually in the United States.

The decision to launch FTA negotiations with South Korea is especially important to us, because this represents the first U.S. effort to negotiate an FTA with a major world steel-exporting nation since the inception of the NAFTA.

The ROK government has supported and “targeted” Korea’s steel industry as a “strategic” sector for decades, and this industry has a long history of close ties to both the Korean government and military. Today, South Korea has the fifth largest steel industry in the world. The Pohang Iron and Steel Company (POSCO), until recently government-owned and controlled, is the fifth largest steel company in the world. According to OECD data, in 2005, South Korea’s steel capacity was around 53.3 million metric tons (MT); its domestic steel demand was about 46.9 million MT; and its steel exports to the world were roughly 16.1 million MT (2.2 million net tons of which went to the U.S market.).

While all U.S.-ROK steel trade (not affected by trade cases) is already tariff-free, having zero tariffs is not, by itself, a “primary driver” of U.S.-Korea trade in steel. It does not lead automatically to increased U.S. imports of ROK steel, and it certainly does not mean that U.S. exports of steel will increase to Korea (steel imports from the U.S. currently represent less than one percent of Korea’s total steel imports). Instead, when it comes to steel trade with Korea -- and Asia in general -- it seems that there are other, more important factors at work than the level of bound or applied normal duty rates. Steel trade flows are affected more by NTBs and by macroeconomic developments -- including the extent to which excess steel capacity in South Korea and other Asian nations is, or is not, able to find a “home” in China or other major world export destinations.

The main problem appears to be that trade in steel or other “strategic” sectors can be very “free on paper” with the ROK and other Asian countries -- yet “free on paper” will not result in any measurable gains in U.S. trade performance. This is why so many of the U.S. steel industry’s domestic customers, especially small and medium-sized firms, have now concluded that the only way to achieve bottom line “results” in trade with the mercantilist countries of Asia is through numerical -- and enforceable -- targets, i.e., managed trade.

With regard to steel and the ongoing mercantilist policies of the ROK government, our concern stems from a decades-long history of South Korean government support for the steel sector, promotion of steel exports and resulting injurious unfair trade by Korean steel firms. In the July 2000 U.S. Department of Commerce (DOC) report entitled “Global Steel Trade: Structural Problems and Future Solutions,” the report’s Korea chapter highlighted (1) the problem of “unsound, often government-influenced, bank lending practices” and (2) the “fundamental concerns about competition within the Korean steel market ...”. The most recent National Trade Estimates (NTE) Report (2004) reaffirms a continuation of Korea’s “*undue reliance on exports, particularly from its traditional export-oriented industries, such as automobiles, semiconductors and steel.*”

As explained in the "Global Steel Trade" DOC report, during the 1997-98 Asian financial crisis, the bankrupt and un-creditworthy Hanbo Steel became a "poster boy" in South Korea for the political and economic corruption, and the state-directed preferential financing, which were among the leading causes of the economic meltdown in Asia in the first place. In 1997-98, Korea was a major contributor to the record surge of injurious and unfairly traded steel in the U.S. market. In the years following the crisis, there have continued to be periodic surges of dumped and subsidized steel from South Korea. Notwithstanding the privatization of POSCO, it and other ROK steel firms have continued to benefit from direct and indirect government subsidization (including "dual pricing schemes" for flat rolled steel going into tubular products).

In the year 2000, the United States registered a 3.0 million net ton (NT) steel trade deficit with South Korea. In 2005, the U.S. steel trade deficit with Korea was "only" 2.2 million NT. This "improvement" was not the result of zero tariff treatment on steel imports in South Korea. Rather, it was due to the successful prosecution of steel trade cases in the United States. In addition to the antidumping (AD) or countervailing duty (CVD) steel "orders" against South Korea that have existed in the recent past (e.g., on cold rolled flat products, structural beams and steel wire rope), there are current unfair trade orders against Korea in the following key steel product lines:

- Cut-to-length plate;
- Corrosion resistant flat rolled;
- Concrete reinforcing bar;
- Oil country tubular goods;
- Circular welded non-alloy steel pipe;
- Stainless angles, wire rod, bar, plate in coils and sheet and strip in coils.

What this history of unfair trade in steel tells us is that, in any FTA with the ROK:

- The U.S. should not agree to any proposal that would weaken in any way U.S. trade remedy laws or trade law rights. This is a bedrock principle for the U.S. steel industry, and any departure from it would cause us to oppose this or any other proposed FTA.
- The U.S. should not agree to any process similar to the NAFTA Chapter 19 dispute settlement system, whereby binational panels are permitted to hear cases and sit in judgment of U.S. law in AD/CVD appeals. In addition to constitutional concerns, repeated questions have arisen about bad decisions, judicial activism and impartiality or expertise of panelists. Accordingly, our U.S. members join with other U.S. trade law-using industries to insist that neither the KFTA nor any other proposed U.S. FTA include international dispute settlement provisions that would or could supplant existing U.S. law, courts and procedure for the review of trade remedy determinations.

- The U.S. should insist upon the NAFTA rules of origin (ROO) for steel products and strict ROO for manufactured products in general. We support the steel ROO in the NAFTA and, regarding steel ROO in a KFTA, does not wish to see any departure from the sound and effective NAFTA ROO. Unfortunately, in two recent FTAs -- the Central American Free Trade Agreement (CAFTA) and the U.S.-Peru FTA -- the U.S. agreed to accept more lenient and flexible steel ROO than exist in the NAFTA. It is our view that, in any KFTA, the U.S. should insist on: (1) the NAFTA ROO for steel products -- so as to avoid conferring origin based merely on rolling or minor processing operations in an FTA country; and (2) strict ROO across-the-board on manufactured products -- so as to (a) avoid conferring FTA benefits based on a relatively lesser amount of processing in an FTA country, (b) ensure that the benefits go where they are intended and (c) ensure that the FTA not serve to incentivize and benefit products where value is added largely or substantially in third countries.

II. Non-tariff Barriers and Indirect Steel Trade: History of Lack of Access for U.S. Producers of Steel-Containing Products

“Indirect” steel trade is imports vs. exports of cars, machinery and other steel-containing products, expressed in tons of steel. In year 2004, according to data developed by our organizations, the United States ran an estimated indirect steel trade deficit with South Korea of approximately one million NT -- up from 600,000 NT in 1999. A key reason why it is so difficult to improve America’s indirect steel trade balance with the ROK is the historic lack of access in the Korean market for U.S. (and other foreign) producers of steel-containing manufactured goods.

The history of U.S.-ROK trade in motor vehicles provides a good case study on the major market access challenge facing U.S. manufacturers that want to sell in Korea. In the case of vehicles, the two governments previously negotiated two separate agreements (in 1995 and 1998), which were intended to open up Korea’s auto market. The result has been that, in 2005, approximately 4,000 U.S.-made autos were sold in South Korea (about the same number sold in 1996); meanwhile, Korean auto sales in the U.S. surged from 136,000 in 1996 to more than 730,000 units last year. The ROK automotive market remains effectively closed to imports from the U.S. and elsewhere due to a complex range of written and unwritten tariff and non-tariff barriers to trade.

Unless the proposed U.S.-Korea FTA (KFTA) is “done right” -- which means effectively addressing all of Korea’s tariff and non-tariff barriers to imports of steel-containing products -- there can be no measurable progress for steel’s U.S. customers under a KFTA. Given the size of South Korea’s manufacturing sector and the failed Korean track record when it comes to providing real market access to U.S. producers of automotive and other steel-containing products -- we urge that, in any KFTA, there must be:

- An end to all Korean NTBs that have limited imports of U.S. (and other foreign) manufactured goods and a process to ensure that no new NTBs are introduced;
- An end, in particular, to Korea's "double testing" requirements and to the use of standards and certification procedures as NTBs;
- Full transparency in regulations and rulemaking in the ROK;
- Full disclosure and discipline regarding ROK government direct -- and indirect -- subsidies to manufacturing in Korea, given a history of "industrial targeting" of steel, autos and other "strategic" sectors by the government of South Korea;
- A level playing field in the structure and application of ROK domestic tax policy -- e.g., an end to the eight separate taxes, in addition to tariffs, which imported autos are currently required to pay;
- Enhanced transparency and due process procedures for covered government procurement entities in the ROK -- but no expansion of covered entities in the KFTA, given the continued lack of equity and results for U.S. firms in this area to date;
- Stronger provisions on competition policy than exist in all previous FTAs, given a history of illegal cartel and other anticompetitive practices by the Korean Chaebol banks, steel producers and others key players in Korea's economic development;
- Stronger provisions on intellectual property rights (IPR) protections as well, given a history of ROK government toleration of IPR violations;
- Iron clad enforcement provision for all of the key ROK commitments.

III. "New" Issues: Exchange Rate and VAT Manipulation

The recent history of FTAs shows that they can be used to expand our traditional thinking about trade and to address important "new" issues -- including labor and environment standards, investment rules and antitrust cooperation. With regard to the proposed KFTA, we are of the view that it must address two key issues that have a huge impact on trade flows, but which historically have not been part of FTAs -- namely, government manipulation of (1) exchange rates and (2) value-added taxes (VATs).

On the currency issue, this FTA must include principles and provisions that would: (1) commit the Korean government to a market-determined exchange rate and a free-floating won; limit the accumulation of ROK currency reserves (at present, more than \$215 billion) to those necessary and prudent to support the won and Korean commercial banks; (3) provide appropriate sanctions for variance from these disciplines; and (4) disallow "escape hatches" that would enable the ROK government to evade these commitments

While the precise shape or definition of such currency provisions remain to be determined, we are convinced that it will be possible to address this critical issue of currency effectively in the KFTA, just as so many other difficult "new" issues have been addressed in previous FTAs. Given the history of currency manipulation by the ROK

government to keep the value of the won at an artificially undervalued rate³, effective currency provisions are essential in this FTA.

On the issue of border-adjustable taxes (BATs), we recognize that this is part of a much broader problem (see below). However, the KFTA should, at a minimum, commit the ROK government to refrain from increasing BAT rebates on South Korean exports (which function as subsidies) once this FTA goes into effect.

IV. Broader Trade Context

Our position on new FTAs has historically been that we support such initiatives to liberalize trade, with the goal of increasing market access for U.S. manufacturers -- as long as they enhance, and do not weaken in any way, U.S. trade laws or trade law rights. Unfortunately, it has become increasingly clear to us in recent years that FTAs alone will do little to reverse the dangerous and unsustainable, record U.S. trade deficits. The United States today is running massive trade deficits both with FTA and non-FTA countries, and there is little reason to expect that an FTA with Korea will reverse the current significant U.S. trade deficit (\$16.9 billion in 2005) with that country.

With the U.S. trade deficit now approaching 6-7 percent of GDP and, with global trade imbalances becoming worse, our domestic manufacturing base has already suffered serious damage -- and U.S. national and economic security is being put at risk. The United States should not wait until a full-blown national and global economic crisis is at hand. If our nation is to reverse these dangerous trends, we need to:

1. Understand the extent to which our massive trade deficits are self-inflicted;
2. Get our own economic house in order -- e.g., by increasing our national savings rate, addressing our federal budget deficit and eliminating excessive regulatory and other cost burdens on U.S. manufacturing;
3. Change the direction of U.S. trade policy.

A business-as-usual approach to trade -- and pat assumptions that America can somehow export its way out of this unsustainable trade deficit -- will not work. It also will not help to allow this problem to descend into a false battle between "free trade" and "protectionism." A public that does not believe trade is fair will not support trade liberalization. We cannot continue to negotiate new FTAs in the absence of close monitoring and measurement of the results of past FTAs. The public also expects the U.S. government to pay as much attention to the import, as it does to the export, side of the trade ledger. In short, we require a more effective, results-oriented trade policy. A good place to start would be to focus, in a bipartisan way, on three "big picture" issues:

³ The U.S. Treasury Department actually cited the ROK government for currency manipulation in October 1988, in April 1989 and in October 1989.

- First and foremost, because strong and strictly enforced trade laws remain an essential underpinning of any pro-manufacturing policy, the United States must resist all WTO Doha Round efforts to weaken the current international “rules” against dumping and trade-distorting subsidization. The ROK government has been one of the so-called “Friends of Antidumping Negotiations (FANs), which has been pushing hard in Geneva for trade law weakening changes in the WTO rules negotiation. It is critical that U.S. negotiators make it clear to the ROK, China, Japan and other governments in no uncertain terms that the U.S. Administration will not accept -- and the U.S. Congress will not approve -- any Doha Round package that weakens America's vital laws against unfair trade, as outlined in S. Con. Res. 55, which passed the United States Senate by voice vote in 2005 as an amendment to a tax reconciliation bill.
- Second, because manufacturers in the United States cannot compete against foreign governments that intervene excessively in exchange markets to keep their currencies at severely undervalued rates in order to obtain artificial trade advantages, we need to enact -- and use -- new trade remedy tools to counter currency manipulation by Korea and other foreign governments. In this regard, it is also essential to recognize that, as long as one major country (China) retains the most severely undervalued major currency in the world, other nations (including Korea and Japan) will feel compelled to maintain their currencies at an artificially undervalued rate.
- Third, because manufacturers in the U.S. cannot compete against an OECD-average 18 percent government VAT rebate on other countries’ exports of manufactured goods in world markets, we need to address the adverse trade impacts of today’s un-level international playing field in the area of taxation. The U.S. can no longer afford to accept discriminatory WTO rules that allow the European Union (EU) and other countries to border-adjust their indirect taxes (rebate such taxes on exports and apply them to imports), while it prevents the United States (which relies primarily on direct taxes) from border-adjusting its taxes. The latest adverse WTO ruling on the U.S. “JOBS” (FSC/ETI replacement) bill should be a wake up call for the United States to make it a top trade negotiating priority to fix, once and for all, this fundamental WTO tax inequity. This is a trade, more than a tax, issue, and the U.S. must insist, in the current WTO “Rules” negotiation, that the WTO prohibit all border-adjustable taxes.

V. Conclusions

AISI, SMA, SSINA and our U.S. member companies will closely monitor the KFTA negotiation, and we urge the Steel Caucus and entire Congress to do the same.

Insofar as Korea is negotiating FTAs simultaneously with all three NAFTA countries -- and recent newspaper articles have talked about the ROK goal of using a new FTA with Mexico, for example to gain increased access to the U.S. market -- AISI, SMA and SSINA

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on behalf of our North American membership, also urges that the U.S. government consult closely with the governments of Canada and Mexico on KFTA issues to the extent possible.

Our final position on the U.S.-Korea FTA, on behalf of U.S. member companies, will be determined in the end by several factors, including the extent to which:

- The strength of U.S. AD/CVD laws is fully maintained, not only in the KFTA, but also in the WTO Doha Round rules negotiation;
- NTBs on steel and steel-containing manufactured goods are effectively eliminated in the KFTA, and no new NTBs on these products are reintroduced;
- The United States effectively addresses the "new" issues of currency and BAT manipulation, both in the KFTA and in other negotiating arenas as appropriate -- e.g., on currency, through direct talks with offending governments and, on BATs, through the Doha Round negotiation on rules.

We appreciate this opportunity to provide written comments to the ITC on the proposed FTA with the Republic of Korea and the probable economic effect of providing duty-free treatment for imports

Sincerely,



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