

**Written and Oral Statement of Nova J. Daly**  
**Before the U.S.-International Trade Commission**  
**Hearing on Trans-Pacific Partnership Agreement: Likely Impact on the U.S. Economy and**  
**on Specific Industry Sectors**  
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I want to thank Chairman Broadbent and Vice Chairman Pinkert and the Commissioners here today for providing me with the opportunity to briefly discuss the strengths and weaknesses of Chapter 17 of the Trans-Pacific Partnership Agreement (“TPP”) regarding State-Owned Enterprises (“SOE”) and Designated Monopolies and its utility to U.S. businesses.

Having worked in government for nearly 10 years and now in the private sector, there are few issues that I have seen rise to such prominence in trade and investment policy discourse as addressing competition from SOEs and state-supported actors. And I suspect this issue comes frequently to your attention in your roles as Commissioners of this august body.

American companies have raised their voices and concerns regarding potential unfair competition from SOEs, and the government has taken positive action, especially as these concerns are well founded. Market distortions and unfair competition caused by SOEs has led to the peril of key U.S. industries. Further, in a number of cases, the home governments from which these SOE’s reside inevitably take on unsustainable debt in their efforts to support unfair SOE competition. U.S. companies have and are improperly losing domestic and international sales to subsidized SOEs, and I have seen numerous investment transactions where foreign SOE’s have outbid all U.S. and private sector actors.

The U.S. began to address this problem with the Singapore FTA agreement and then with sovereign wealth funds through the *2008 Generally Accepted Principles and Practices* (“Santiago Principles”), and now with the TPP. Efforts to address unfair SOE competition should continue in other matters such as the Trans-Atlantic Trade and Investment Partnership,

bilateral investment treaties, and other bilateral, plurilateral and multilateral agreements, such as the Trade in Services Agreement (“TISA”).

For some of the TPP nations we know that their SOEs represent sizable portions of their GDP. For instance, in Vietnam, SOEs account for 1/3 of the countries’ GDP. For Singapore and Malaysia that number is 15%. So the inclusion of the SOE chapter in the TPP is an important and helpful step forward in U.S. trade and investment policy as it creates new disciplines to address the potential negative economic implications of SOE trade and investment. In creating such disciplines, the Chapter moves beyond the Santiago Principles in creating enforceable rules and builds toward globally accepted conduct for SOEs operating in domestic and international marketplaces. The Chapter’s basic rules are that SOEs:

- Operate in accordance with commercial considerations;
- Comply with national treatment and most favored nation principles in their commercial operations; and
- Operate without receiving or providing non-commercial government assistance.

These basic rules serve as important statements of principle which SOEs and their host governments should themselves welcome when operating in the marketplace as quasi-competitive commercial entities.

In a number of economic sectors, there is clear evidence of the detrimental effects to private actors that have arisen as a result of SOE activity. The trade effects have been particularly severe in basic materials such as steel and aluminum, where governments have relied on loss-making SOEs to provide employment, tax revenue, and other economic contributions. Government backing shields these SOE firms from bankruptcy and ultimate exit from the market, resulting at times in intractable overcapacity and adverse effects that spread throughout the global economy. SOEs have also become increasingly active in foreign investment, raising

not only economic but also important national security considerations. SOE investments abroad are sometimes carried out with extensive financial support from home governments.

Chapter 17 of the TPP is useful in seeking to address these issues, however, it carries some notable weaknesses. For instance, the narrowness of the Chapter's definition of SOEs and the breadth of the exemptions in the Chapter's annexes may render some of its disciplines unenforceable. First, the chapter defines SOEs to include only enterprises "principally engaged in commercial activities" and in which a government (i) directly owns more than 50 percent of the share capital; (ii) controls, through ownership interests, more than 50 percent of the voting rights; or (iii) holds the power to appoint a majority of the members of the board of directors. The desire for clear definitions is understandable, but this limitation to majority ownership in practice can permit governments to avoid the chapter's disciplines, while maintaining effective control over nominally commercial enterprises. In the solar energy industry, for example, identical distortions arise as nominally private firms in targeted industries enjoy close connections to the state and extensive support from government entities such as policy banks and other state-owned financial institutions.

Other U.S. trade agreements provide guidance for broadening the definition of SOE without sacrificing clarity. The U.S.-Singapore FTA, for example, defines "government enterprises" to include any entity in which the government has "effective influence." This includes not only majority ownership, but also "the ability to exercise substantial influence" over certain types of corporate decision making.<sup>1</sup> There is a rebuttable presumption of effective influence when the government owns more than 20 percent (but less than 50 percent) of an

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<sup>1</sup> U.S.-Singapore FTA at Art. 12.8(5).

enterprise's voting securities and accounts for the largest block of the enterprise's voting rights.<sup>2</sup> This definition recognizes the reality that governments may exert controlling influence over commercial entities through channels other than majority share ownership.

Second, Annex 17-D to the Chapter provides expansive exemptions from rules governing commercial considerations, non-discrimination, and non-commercial assistance for sub-central SOEs for all Parties.<sup>3</sup> Exempting sub-central SOEs from these critical disciplines simply because they are not owned by the central government creates a potentially significant loophole. At the least, disciplines should have been applied to these entities where they operate in the markets of other TPP Party members.

Another important consideration is the Chapter's transparency rules, which are valuable on their face. The rules allow Parties to request information relating to government ownership and voting rights, the identities of government officials acting as company officers or board members, the company's annual revenues, legal exemptions and immunities, and non-commercial assistance. However, the rules on transparency may not provide much comfort given the broad discretion governments have to claim confidential treatment for information provided in response to requests from other Parties. While legitimate business proprietary and national security information must be protected, transparency rules should aim not only to increase transparency among governments, but also to increase transparency among the general public and the companies that must compete with SOEs in global markets. Parties should not be able to claim confidential treatment simply to avoid public scrutiny of clear violations of the chapter's disciplines, to prevent information from being used as evidence in trade remedies proceedings, or otherwise to prevent legitimate remedial action from being taken. Any request

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<sup>2</sup> *Id.*

<sup>3</sup> TPP at Annex 17-D.

for confidential treatment should be justified by a clear need to protect proprietary information or information related to the national security of the Party responding to the request.

In closing Chapter 17 is helpful, but lacking. However, there are opportunities to expand SOE coverage and disciplines in future agreements, such as the TTIP, the TISA, and the U.S. – China Bilateral Investment Treaty. For the TPP, although the rules cannot be changed now as a practical matter, improving them should continue to be a top priority in any further negotiations pursuant to TPP Annex 17-C.