I. INTRODUCTION

As of the end of 2011, 427 disputes had been lodged with the WTO's Dispute Settlement Body.[1] However, the number of complaints continues to decline, from an average of 37 complaints per year during the period 1995 through 1999, to 27.8 during the period 2000 to 2004, to 15.6 from 2005 to 2009, and 12.5 from 2010 to 2011.[2] Appeals (in original appeals and Article 21.5 cases)[3] had been filed, and the Appellate Body had issued decisions, in 105 as of the end of 2011.[4] Over a sixteen-year period (1995–2011),[5] the number of Appellate Body reports issued per year has declined, ranging from 6.2 per year during the period 2000 through 2004, to 3.5 per year from 2010 through 2011.[6] Since 1995, approximately 68% of the panel reports have been appealed.[7]

What is atypical is the length and complexity of some of the cases, particularly *EC – Airbus*.[8] The strains on the Appellate Body and its secretariat were evident in the fact that several Members lodging appeals agreed to defer those appeals. Thus, in both *US – Tyres*[9] and *EC – Fasteners*,[10] the Complainant

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1. Kara Leitner & Simon Lester, *WTO Dispute Settlement 1995-2011 – A Statistical Analysis*, 15 J. INT'L ECON. L. 315, 321 (2012); *see Chronological List of Disputes Cases*, WORLD TRADE ORG., http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm (last visited Sept. 15, 2012).

2. *See* Leitner & Lester, *supra* note 1, at 316 (providing historical statistics on use of the Dispute Settlement Body).

3. Article 21.5 provides in pertinent part, "Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel." Understanding on Rules and Procedures Governing the Settlement of Disputes, art. 21, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401 [hereinafter DSU]. Article 21.5 decisions are not reviewed in this series.

4. *Dispute Settlement: Statistics*, WORLD TRADE ORG., http://www.wto.org/english/tratop_e/dispu_e/stats_e.htm (last visited Sept. 15, 2012).

5. While the DSU has been in operation since Jan. 1, 1995, no appeals reached the Appellate Body until 1996. *See id.*; Leitner & Lester, *supra* note 1, at 321.

6. Leitner & Lester, *supra* note 1, at 321.

7. *Id.*

8. *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/AB/R (May 18, 2011) (*adopted* June 1, 2011) [hereinafter Appellate Body Report, *EC – Airbus*]. The Panel Report in this case is Panel Report, *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/R (June 30, 2010) (*adopted as modified* June 1, 2011) (complaint by the United States) [hereinafter Panel Report, *EC – Airbus*]. For a discussion of this Appellate Body Report, see *infra* Part II.C.

9. Panel Report, *United States – Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China*, WT/DS399/R (Dec. 13, 2010) [hereinafter Panel Report, *US – Tyres*]; Appellate Body Report, *United States – Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China*,

(China) and the Respondents (United States, European Union) agreed to extend the deadlines for the filing of appeals to May 24 and March 25, respectively.[11] The reason given was the additional time required for the Appellate Body (beyond the normal ninety days) as a result of the extreme complexity of the *EC – Airbus* case and the perceived need by trade diplomats to avoid new appeals until the report in *EC – Airbus* was issued (in May).[12] This is not unprecedented; several appeals were similarly delayed in 2005 and 2007.[13] The backlog continued into 2012, with the appeals in *US – Aircraft*[14] (which normally would have been issued within ninety days of the notice of appeal, June 30, 2011) and *China – Raw Materials*[15] (the ninety-day period ending November 28) both delayed into 2012.[16] By January 2012, Canada, the United States, and Mexico had agreed on a delay in the expected appeal of the Panel Report in *US – COOL Requirements*, which the appellate report ultimately adopted in July 2012.[17] Also, the Appellate Body failed to issue its typical annual report in 2011.

WT/DS399/AB/R (Sept. 5, 2011) (*adopted* Oct. 5, 2011) [hereinafter Appellate Body Report, *US – Tyres*]. For a discussion of this Appellate Body Report, see *infra* Part II.E.

10. Panel Report, *European Communities – Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China*, WT/DS397/R (Dec. 3, 2010) [hereinafter Panel Report, *EC – Fasteners*]; *European Communities – Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China*, para. 2, WT/DS397/AB/R (July 15, 2011) (*adopted* July 28, 2011) [hereinafter Appellate Body Report, *EC – Fasteners*]. For a discussion of this Appellate Body Report, see *infra* Part II.B.

11. Daniel Pruzin, *Safeguards: U.S., China Agree to Suspend Appeals Proceedings in WTO Tire Safeguard Dispute*, 28 INT'L TRADE REP. (BNA) 190 (Feb. 3, 2011).

12. *Id.*; *see* Appellate Body Report, *EC – Airbus*, *supra* note 8.

13. *See Heavy DSB Workload Forces U.S., China to Delay Action on Tire Panel*, WORLD TRADE ONLINE, Feb. 10, 2011, http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade-02/11/2011/heavy-dsb-workload-forces-us-china-to-delay-action-on-tire-panel/menu-id-710.html (reporting on the delays in a tire dispute between the EU and Brazil in 2007 and a sugar dispute between the EU and Australia in 2005).

14. Panel Report, *United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)*, WT/DS353/R (Mar. 31, 2011) (with appeal filed by the United States on April 28, 2011, *Notification of an Other Appeal by the United States*, WT/DS353/10 (Apr. 29, 2011); Appellate Body Report, *United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)*, WT/DS353/AB/R (Mar. 12, 2012) (*adopted* Mar. 23, 2012).

15. Appellate Body Report, *China – Measures Related to the Exportation of Various Raw Materials*, WT/DS394/AB/R, WT/DS395/AB/R, WT/DS398/AB/R (Jan. 30, 2012) (*adopted* Feb. 22, 2012).

16. *Understanding the WTO: Settling Disputes: A Unique Contribution*, WORLD TRADE ORG., http://www.wto.org/english/thewto_e/whatis_e/tif_e/disp1_e.htm (last visited Sept. 15, 2012); Appellate Body Communication, *United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)*, WT/DS353/12 (Mar. 13, 2012) (announcing the completion of its report); Appellate Body Communication, *China – Measures Relating to the Exportation of Various Raw Materials*, WT/DS398/13 (Feb. 1, 2012) (announcing the completion of its report).

17. Panel Report, *United States – Certain Country of Origin Labeling (COOL) Requirements*, WT/DS384/R, WT/DS386/R (Nov. 18, 2011); Appellate Body Report,

As of January 2012, two new members, Ujal Singh Bhatia of India and Thomas Graham of the United States, joined the Appellate Body after approval of the membership. They replaced Jennifer Hillman of the United States and Lilia Bautista of the Philippines, both of whom announced in mid-2011 that they would not seek reappointment to additional four-year terms when their terms expired.[18] The terms of two of the remaining five members, Shotaro Oshima of Japan and Yuejiao Zhang of China, expired in May 2012; Oshima had announced his retirement,[19] but Zhang is expected to be reappointed for an additional four-year term. Oshima was replaced in May 2012 by Seung Wha Chang, who is the first Korean to sit on the Appellate Body.[20] The terms of other three members, Peter Van den Bossche of Belgium, Ricardo Ramirez-Hernández of Mexico, and David Unterhalter of South Africa continue into 2013.[21] Most appointees have served two terms, as is reflected by the fact that after seventeen years, only twenty-three persons (including the present incumbents) have served on the Appellate Body's seven-member roster. Typically, the seven-member Appellate Body includes members who are nationals of the United States, the EU, Japan, China, and India.

II. DISCUSSION OF THE 2011 CASE LAW FROM THE APPELLATE BODY

A. GATT Obligations

1. Citation

Appellate Body Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines*, WT/DS371/AB/R (June 17, 2011) (*adopted* July 15, 2011) (complaint by the Philippines).[22]

United States – Certain Country of Origin Labeling (COOL) Requirements, WT/DS384/AB/R, WT/DS386/AB/R (June 29, 2012) (*adopted* July 23, 2012); *see* Daniel Pruzin, *Labeling: WTO Backs Delay in Expected U.S. Appeal of Decision Against U.S. COOL Meat Rules*, 29 INT'L TRADE REP. (BNA) 49 (Jan. 12, 2012) (reporting on the agreement by the Dispute Settlement Body).

18. Daniel Pruzin, *WTO Members Approve New Appellate Body Judges*, 28 INT'L TRADE REP. (BNA) 1885 (Nov. 24, 2011).

19. Daniel Pruzin, *WTO: WTO Announces Early Departure of Appellate Body Judge Oshima*, 29 INT'L TRADE REP. (BNA) 87 (Jan. 19, 2011) (reporting on Judge Oshima's retirement as of April 7, 2012).

20. *See* Daniel Pruzin, *WTO: Korean Candidate Chosen to Fill WTO Appellate Body Vacancy*, 29 INT'L TRADE REP. (BNA) 805 (May 17, 2012).

21. *Appellate Body Members*, WORLD TRADE ORG., http://www.wto.org/english/tratop_e/dispu_e/ab_members_descrp_e.htm (last visited Sept. 15, 2012).

22. Hereinafter Appellate Body Report, *Thailand – Cigarettes*. The WTO Panel Report in the case is Panel Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines*, WT/DS371/R (Nov. 15, 2010) (*adopted as modified* July 15, 2011) [hereinafter Panel Report, *Thailand – Cigarettes*]. The third parties in the case were

2. Facts

Before the WTO Panel, the Philippines alleged that Thailand imposed certain discriminatory customs and fiscal measures on imported Philippine cigarettes.[23] The controversial Thai measures included tax and administrative requirements. The Philippines alleged that those measures violated the General Agreement on Tariffs and Trade (GATT) and the WTO Agreement on Customs Valuation (Customs Valuation Agreement). The Philippines prevailed at the Panel stage, but Thailand lodged two appeals with the WTO Appellate Body.

In them, Thailand challenged certain holdings of the Panel concerning GATT Articles III:2 and III:4, the famous and heavily litigated national treatment obligations for fiscal and non-fiscal measures, respectively.[24] The Appellate Body effectively upheld the Panel holdings; i.e., Thailand lost on appeal, too. Thailand invoked the Article XX(d) administrative necessity defense to its national treatment violations, but with no success at either stage. The Appellate Body, in particular, held that Thailand failed to show its measures were "necessary" to support its underlying domestic administrative apparatus.

a. Thai VAT Regime Generally

On appeal, the only controversial Thai measure affecting Philippine cigarettes at issue was the value added tax (VAT) measure.[25] The Thai VAT is

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Australia, China, European Union, India, the United States, and the Separate Customs Territory of Taiwan, Penghu, Kinmen, and Matsu.

23. *See* Panel Report, *Thailand – Cigarettes*, *supra* note 22, paras. 7.1–7.4.

24. *See* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 82. In addition to the Article III appeals, Thailand also challenged a holding by the Panel regarding GATT Article X:3(b). *Id.*

25. The Panel offered two definitions of a "VAT." The first definition was from *Black's Law Dictionary*, an American lexicographic source: "[A] tax assessed at each step in the production of a commodity, based on the value added at each step by the difference between the commodity's production cost and its selling price. A value added tax . . . effectively acts as a sales tax on the ultimate consumer." Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.454 (citing BLACK'S LAW DICTIONARY 1472 (7th ed. 1999)). The second definition came from the Organization for Economic Cooperation and Development in Paris, and it offered more detail:

> [V]alue added taxes (VAT) are consumption taxes. They have three distinctive characteristics: they are levied on a broad base (as opposed to excise taxes, which cover specific products), the collection system is organised in stages where each agent may deduct input taxes on purchases and must account for output tax on sales, and, ultimately, the burden will be borne by consumers who, as end-users, cannot operate immediate deduction operations. In practice, three tax collection mechanisms are mainly used: (a) under a registration system, the vendor registers with the tax authorities and is responsible for

part of and administered through the Thai Revenue Code.[26] According to this Code, all sellers of any good or service in Thailand must apply for VAT registration before selling their good or service. Sellers are exempt from this registration requirement if they sell only VAT-exempted goods or if their business falls below a minimum floor of annual sales.[27] A registered seller is referred to as a "VAT registrant."

For many products, the VAT tax is 7% ad valorem, and Thailand and the Philippines agreed this figure was the pertinent rate in this case.[28] The Thai Revenue Code requires a VAT be imposed on all VAT registrants in the distribution chain of a particular product.[29] Furthermore, as the Appellate Body explained, the "VAT is determined by applying this [VAT] rate to the actual selling price of the product at each stage of the supply chain."[30]

VAT registrants must report VAT monthly, and:

> [They] are [generally] entitled to deduct the "input tax," paid upon purchase of the goods from the previous seller, from the "output tax" collected from the next purchaser of the goods. VAT liability under Thai law in respect of a sales transaction thus consists of the amount to be paid after subtracting input tax from output tax . . . .[31]

In simple arithmetic terms:

[VAT Liability Base] = [Output Tax] – [Input Tax]

For example, consider a three-stage commercial chain involving three parties, *X*, *Y*, and *Z*, and two sales transactions, one from *X* to *Y*, and the other one from *Y* to *Z*. Suppose *Y* purchases an input from *X*, say, cotton fabric, and pays an input tax of US$100. *Y* then uses the cotton fabric to manufacture a T-shirt, which *Y* sells

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> paying/collecting the tax; (b) the tax may, alternatively, be collected directly by the customs authorities at the border; (c) under the reverse charge/self-assessment system, the customer pays directly to the tax authorities.

Id. (citing ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, INTERNATIONAL VAT/ GST GUIDELINES 7 (2006)).

26. *See* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 86. *See also* Act Promulgating the Revenue Code, B.E. 2481 (1938) (Thai.) (Panel Exhibit PHL-94). The Appellate Body Report refers to this Act as the Thai Revenue Code. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 86.

27. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 86 n.97.

28. *See* Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.457; *see also* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 86.

29. Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.457.

30. *Id.*

31. *Id.* (footnotes omitted).

to *Z*, a retail store. *Z* pays an output tax of $500. What is the basis on which Thai authorities compute the VAT liability of *Y* under the Code?

The answer is the difference between the output tax and input tax, which in this example is $400. The actual VAT liability that *Y* would be obliged to pay would be 7% (the VAT rate) of $400, or $28. Note that under the Thai VAT scheme, when the input tax is higher than the output tax the difference is treated as a VAT credit, and the seller may receive a refund of the difference or apply it against future VAT assessments.[32]

b. Cigarettes Under the VAT Regime: Reference Pricing

The Thai VAT regime treats the sale of cigarettes slightly differently from most other products. The Appellate Body outlined two main distinctions:

> First, instead of applying the tax rate [of 7%] against the actual sales price, VAT is determined for each stage of the supply chain for cigarettes, starting with the first sale of cigarettes in Thailand by Thailand Tobacco Monopoly ("TTM") or an importer, by applying the seven per cent rate to the maximum retail selling price ("MRSP"), a reference price fixed by the Thai Government for each brand of cigarettes. This means that, because VAT is based on the same fixed price at each stage of the supply chain, the amount of VAT assessed is the same for each sales transaction along that chain. Moreover, because the VAT paid by a reseller of cigarettes to a prior seller in the form of input tax is the same as the amount that the reseller collects from a subsequent purchaser in the form of output tax, *these amounts will, subject to compliance with certain administrative requirements, be offset, resulting in a VAT liability of zero*.[33]

Unpacking this tax rule (which the Appellate Body failed to do), the first of the above sentences simply indicates that the market price (at any stage in the commercial chain) for cigarettes in Thailand is not the price to which the VAT applies. Rather, the VAT applies to a government-mandated price. The second sentence is the logical consequence of the first. Given that the government establishes a price at each stage of the commercial chain in cigarette sales, for any particular stage, the VAT liability will be the same. Again, actual prices paid in the market do not matter for VAT liability purposes because the tax base for the VAT is the government-determined price. Indeed, the government sets the same

32. *Id.* Note in the above example the distinction between three concepts: 1) the basis on which VAT is computed, 2) the VAT rate, and 3) the VAT liability.

33. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 87 (emphasis added) (footnotes omitted).

reference price for each stage in the commercial chain. That is what the third of the above three sentences confirms.

c. Cigarettes Under the VAT Regime: Exemption

The Thailand Tobacco Monopoly (TTM) is a government organization and the only domestic producer of cigarettes.[34] (Herein is a feature characteristic of many developing countries; namely, the government granting a monopoly to a state-owned enterprise (SOE) to produce cigarettes.) Accordingly, another difference between cigarettes and other goods under the VAT regime is that resellers of domestic cigarettes (i.e., cigarettes produced by TTM) are exempt from the VAT.

Unfortunately, the Appellate Body did not explain clearly the difference between a tax "credit" and a tax "deduction." Yet both terms are used in the Panel and Appellate Body Report, along with the term "exemption." To be clear, a tax "credit" does not affect taxable income. Rather, once tax liability is computed based on taxable income, a tax credit lowers that liability in a dollar-for-dollar sense. In contrast, a tax "deduction" does affect taxable income; namely, it lowers it by the amount of the deduction. Then, tax liability is computed based on the reduced taxable income. Manifestly, a tax credit is more valuable than a deduction because it applies directly to liability, and as its name suggests, "credits" the taxpayer for the amount of the credit, thus reducing the tax bill. In the *Thai Cigarettes* case, the most valuable tax benefit of all was at issue: an exemption. If a taxpayer is eligible for the so-called "VAT exemption," then it means that taxpayer need not pay any VAT at all.

The VAT exemption under the Thai Revenue Code proved to be one of two critical points on appeal.[35] The exemption did not extend to resellers of imported cigarettes, such as those coming from the Philippines. In other words, no VAT was imposed on a resale of domestic cigarettes, but one was imposed on Philippine or any other foreign-originating cigarettes. Thailand ultimately was unsuccessful in defending this measure from allegations concerning GATT 1994 Articles III:2, first sentence, and III:4 (quoted below).[36] To be clear, under no circumstances was a reseller of imported cigarettes ever exempt from VAT liability.

In the absence of an outright exemption, for what might a reseller of imported cigarettes qualify under the Code in an effort to whittle its VAT liability to zero? The answer is it might be allowed to reduce the base on which its VAT liability is taxed by deducting the input tax from output tax. But to qualify for this

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34. *Id.* para. 91. The exemption is provided under section 81(1)(v) of the Thai Revenue Code, section 3(1) of the Royal Decree No. 239 issued under the Thai Revenue Code, and Order No. Por. 85/2542 of the Thai Revenue Department. *Id.* para. 88; *see generally id.* paras. 88–91.

35. *See id.* para. 91.

36. *See id.* paras. 119, 140.

deduction was difficult. Here, then, is the second critical point on which the appeal turned.

The Panel determined that there were six circumstances in which VAT registrants cannot deduct the input tax from the output tax (i.e., six situations in which a taxpayer cannot lower its taxable VAT base by subtracting the input tax from the output tax).[37] The bar on this deduction is significant because it results in higher VAT liability. Recall that VAT liability is the VAT rate of 7% applied to the VAT base, which is the difference between the output tax and input tax. If a registrant cannot deduct the input tax, then as per the above formula, the base on which its VAT is calculated—the VAT Liability—is higher.

Of the six circumstances in which an input tax deduction is forbidden, the Panel identified in the aggregate three of particular importance to the treatment of imported cigarettes. Resellers of imported cigarettes could not obtain an input tax credit if they fail to:

> (i) complete and file the tax form allowing for reporting and payment of VAT on a monthly basis;
> (ii) produce a complete and accurate tax invoice with respect to a transaction; or
> (iii) meet other record-keeping requirements.[38]

Accordingly, the Panel determined that "resellers of domestic cigarettes are *de jure* exempt from the VAT liability, whereas the same exemption is not granted to resellers of imported cigarettes, as tax credits do not automatically and irrevocably offset tax liabilities incurred by [resellers] of imported cigarettes in every case."[39]

The above-quoted passages are poorly thought out. They conflate tax "credits" and "deductions." What the Panel seems to be saying is that the denial to resellers of imported cigarettes of the exemption from paying VAT is not offset in any way. The Thai Revenue Code does not contain an offsetting tax credit (i.e., a dollar-for-dollar, or *baht*-for-*baht*, reduction in the tax bill). The Code does contain an ostensibly offsetting tax deduction (i.e., a reduction in the computation of the VAT tax base, where input tax is subtracted from the output tax). But because of prerequisites that must be satisfied to qualify for the deduction, the deduction is practically meaningless.

In sum, under the Thai Revenue Code, only resellers of domestic cigarettes are automatically and fully exempt from the 7% VAT. In contrast, resellers of imported cigarettes must meet certain preconditions in order to receive zero VAT liability, and these amount to hurdles too high to jump.[40]

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37. *See id.* para. 93.
38. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 94.
39. *Id.* (quoting Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.644).
40. *Id.* para. 95.

d. VAT-Related Administrative Requirements

In addition to addressing issues related to VAT liability, the Thai Revenue Code imposes administrative burdens upon VAT registrants. These requirements are primarily important in the context of the GATT Article III:4 allegation made by the Philippines. According to the Code, if a seller is exempt from VAT liability (i.e., a reseller of domestic cigarettes), then the seller is also exempt from certain VAT administrative requirements.[41]

The Panel identified three VAT administrative requirements (which are similar, but not identical, to those mentioned above) that applied only to resellers of imported cigarettes.[42] To summarize these requirements, resellers of imported cigarettes: (i) must file a tax return every month; (ii) keep records pertaining to input taxes, output taxes, and "goods and raw materials"; and (iii) may incur penalties for non-compliance.[43]

On appeal, Thailand disputed the decisions by the Panel that the VAT exemption for domestic cigarettes violates Articles III:2, first sentence, and III:4.[44] Thailand lost both appeals.

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41. *Id.* para. 97.

42. *Id.*

43. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, paras. 98–100.

44. Thailand also appealed the decision by the Panel that Thailand violated GATT Article X:3(b). The Panel held Thailand "fail[ed] to maintain or institute independent review tribunals or procedures for the prompt review of guarantee decisions." *Id.* para. 182. On appeal, Thailand contested the interpretation by the Panel regarding "administrative actions relating to customs matters" and "prompt review." *Id.* paras. 31, 182–185. The Thai Customs measure at issue permitted Thai customs agents to launch an investigation when there is a question about an applied duty rate on a certain good. The goods may be withdrawn during the investigation if the importer "pays 'the amount of the duty declared in the entry by the importer or the exporter' and provided that 'an additional sum of money covering the maximum duty payable on the goods' is deposited as a guarantee." *Id.* para. 187 (quoting Thai Customs Act, B.E. 2469 § 112 (1926) (Panel Exhibit PHL-20)). After an investigation, the Thai customs officials notify the importer of the final duty rate. If the final duty rate is higher than the duty paid at the time of entry and the importer paid a cash guarantee, then the amount owed is drawn from the guarantee already paid by the importer. If the final duty rate is lower than the duty paid at the time of entry, then the importer will receive a refund, plus accrued interest, for the difference. *See id.* para. 188. Generally, importers and exporters may appeal the final duty rate decision before a separate Board of Appeals. *See id.* para. 189.

The Appellate Body upheld the holding of the Panel. *Id.* para. 222. First, the Appellate Body agreed with the Panel that requiring a deposit of a "guarantee" is an administrative action within the meaning of Article X:3(b). *Id.* para. 216. In part, Thailand failed because the Appellate Body said the guarantee is not an "intermediate step," as the Thais had argued. *See id.* para. 215. Instead, the Appellate Body said: "[T]he guarantee is a device allowing, on the one hand, the importer to withdraw their goods from customs, and, on the other hand, securing the payment of the ultimate customs duty." *Id.*

Second, the Appellate Body determined the Panel had not erred in its interpretation of "prompt review." According to the Appellate Body:

3. GATT Article III:2, First Sentence, and Its Scope in Relation to Article III:4: Issue and Holding on Appeal

Article III:2, first sentence, states: "The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products." The Panel held that Thailand violated Article III:2, first sentence. Thailand subjected imported cigarettes to a higher VAT liability than domestic cigarettes because of the Thai VAT exemption for resellers of domestic cigarettes.[45] Thailand appealed, but the Appellate Body upheld the Panel's holding.

On appeal, Thailand made two main arguments regarding the Article III:2 violation. First, Thailand claimed the measure at issue was administrative, not fiscal.[46] Thailand offered this argument to escape Article III:2 liability. If the VAT exemption were an administrative matter, then it would not fall within the scope of Article III:2, which concerns only internal taxation. That is, Thailand argued the measure was an administrative requirement and, therefore, subject only to the discipline of Article III:4. Thailand's contention was bold: administrative requirements and the fiscal consequences for non-compliance with those requirements are outside the scope of Article III:2. That was true, said Thailand, even though those requirements concern taxation. At bottom, Thailand sought to distinguish between taxation per se, which fell within Article III:2, and the administrative rules associated with taxation, which landed outside Article III:2.

Thailand also reminded the Appellate Body that both imported and domestic cigarettes are subject to a 7% ad valorem VAT rate. Accordingly, Thailand argued that "the Panel's finding was not based on the tax burden under Thai VAT law, but instead was based solely on the difference in the 'administrative requirements' for resales of imported and domestic cigarettes, and the consequences of failure to comply with those requirements."[47]

> In providing that a guarantee can only be challenged once the notice of assessment has been issued, Section 112 of the Thai Customs Act invariably delays review of guarantee decisions and thereby shields guarantee decisions from challenge throughout the period in which they serve as a security and in which traders are most affected by these decisions.

Id. para. 221. Thus, in accordance with the findings of the Panel, the Appellate Body stated: "Thailand's system for the review of guarantee decisions is not compatible with the obligation under Article X:3(b) to provide for the prompt review of administrative action relating to customs matters because such review is not available until after the final assessment of customs duty has been made." *Id.* para. 222.

45. *See* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 118.
46. *Id.* para. 105.
47. *Id.* para.107 (citing Thailand's appellant's submission).

The Philippines rejected the Thai argument and urged the Appellate Body to uphold the decision by the Panel. To the Philippines, the distinction Thailand sought to make was one with no difference: both the VAT tax and its administrative requirements concerning exemptions and deductions were governed by Article III:2.

Second, Thailand claimed that even if the measure were deemed to fall within the scope of Article III:2, first sentence, the measure still adheres to WTO rules.[48] According to Thailand: "[A] system of offsetting input tax against output tax cannot be said to be WTO-inconsistent 'simply because private parties are required to comply with certain administrative requirements,' or because it compels resellers 'to limit claims for input tax credits to actual, legitimate purchases' of cigarettes."[49]

Thailand asserted that "the Panel's finding would limit the ability of WTO Members to ensure the proper administration of their tax regimes."[50] The Philippines rebutted this second Thai argument by emphasizing that the resellers of domestic cigarettes were not subject to the same preconditions regarding zero VAT liability and instead received an automatic VAT exemption.[51]

Before beginning its GATT Article III:2 analysis, the Appellate Body addressed and rejected the characterization by Thailand of the VAT measure. According to the Appellate Body, the description of the measure by Thailand was "under-inclusive and over-inclusive."[52] It was underinclusive because Thailand failed to acknowledge the automatic VAT exemption for resellers of domestic cigarettes. The fiscal implication of the VAT exemption is important to recognize: under certain circumstances, the exemption causes imported cigarettes to incur a higher tax burden than domestic cigarettes.

The Appellate Body deemed the Thai characterization overinclusive because there were only two measures the Panel considered in its analysis of the Philippine claims under Articles III:2 and III:4. Those measures were 1) the VAT exemption for resellers of domestic cigarettes, and 2) the VAT liability incurred by resellers of imported cigarettes that fail to receive the necessary deduction of the input tax from the output tax to reduce or eliminate their VAT liability.[53]

The analysis by the Appellate Body revealed no new developments regarding Article III:2, first sentence. Referring to the 1997 *Canada – Periodicals* case, the Appellate Body noted that Article III:2, first sentence, "applies to a broad range of measures."[54] Then, in a subtle reference to its 1996 *Japan – Alcoholic Beverages II* decision, the Appellate Body reiterated that no de minimis exception

48. *See id.* para. 105.
49. *Id.* para. 117 (quoting Thailand's appellant submission).
50. *See* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 118.
51. *See id.* para. 115.
52. *Id.* para. 108.
53. *See id.*
54. *Id.* para. 112 (citing Appellate Body Report, *Canada – Certain Measures Concerning Periodicals*, at 19, WT/DS31/AB/R (June 30, 1997) (*adopted* July 30, 1997)).

exists to this rule, and "even the smallest amount of 'excess' is too much."[55] The Appellate Body declared:

> For purposes of our consideration of Thailand's appeal, a measure that subjects products to internal taxes or other internal charges may be examined under Article III:2, first sentence, of the GATT 1994. When such a measure subjects imported products to taxes or charges in excess of those applied to like domestic products, it will be inconsistent with the first sentence of Article III:2.[56]

This statement relies on well-established precedent. It does not stray from previously held understandings of Article III:2, first sentence, nor (in the interests of certainty and predictability) should it.

The Appellate Body quickly rejected the first argument Thailand presented. The Appellate Body said the measure is subject to Article III:2 because it is not solely administrative and because it affects the amount of VAT liability imposed on imported and domestic cigarettes.[57] In a footnote, the Appellate Body stated that a measure that is solely administrative still may be subject to Article III:2 if that measure imposes internal taxes or charges on imported and like domestic products.[58] The Appellate Body emphasized that under the VAT exemption, resellers of domestic cigarettes never will be subject to VAT, whereas resellers of imported cigarettes are subject to VAT unless they qualify for the input deduction that could cut or eliminate VAT liability.[59]

In brief, the Appellate Body ruled that a measure that is purportedly only administrative in nature still comes within the ambit of GATT Article III:2 if that measure affects the burden of taxation. In effect, such a measure is not "only" administrative. That measure bears on the level of taxation imposed on domestic versus imported goods. While the Appellate Body rendered this holding in the context of the first sentence of Article III:2, it seems reasonable to forecast that it would do so under the second sentence of that provision, too.

The Appellate Body also rejected Thailand's second argument. According to the Appellate Body:

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55. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 112. *See* Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, at 22, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R (Oct. 4, 1996) (*adopted* Nov. 1, 1996). Recall that any non-de minimis difference in internal taxation violates Article III:2, first sentence (which covers like products). However, a de minimis difference would not violate Article III:2, second sentence (which covers directly competitive or substitutable products).

56. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 112.

57. *Id.* para. 114.

58. *See id.* para. 114 n.144; *see also* Panel Report, *Argentina – Measures Affecting the Export of Bovine Hides and the Import of Finished Leather*, para. 69, WT/DS155/R (Dec. 19, 2000) (*adopted* Feb. 16, 2001).

59. *See* Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 114.

> [I]t is not the mere imposition of administrative requirements that creates a differential tax burden, but rather that only resellers of imported cigarettes will incur VAT liability as a consequence of failing to offset output tax. Resellers of imported cigarettes are subject to VAT liability in defined circumstances under Thai law, whereas resellers of domestic cigarettes, due to a complete exemption from VAT, are not.[60]

The Appellate Body explicitly restated its finding in its 2001 *Korea – Various Measures on Beef* decision: "[T]he intervention of some element of private choice does not relieve Korea of responsibility under the GATT 1994 for the resulting establishment of competitive conditions less favourable for the imported product than for the domestic product."[61]

Under the Thai measure, domestic cigarettes are automatically exempt from VAT liability. So, although the Thai measure included conditions that allowed resellers of imported cigarettes to avoid VAT liability, there exist some circumstances when the imported cigarettes incur a VAT, unlike domestic cigarettes.

Finally, the Appellate Body observed that it was not the existence of administrative requirements that triggered the Article III:2, first sentence, violation. Instead, the Panel correctly found that the Thai measure violated Article III:2 because the preconditions to obtain zero VAT liability pertain only to imported cigarettes. In contrast, domestic cigarettes enjoy "automatic[] and irrevocabl[e] offset tax liabilities . . . in every case."[62] Thus, according to the Appellate Body: "Imposing legal requirements that result in tax liability on imported products when resellers do not satisfy prescribed conditions necessary to avoid that liability, but which never result in tax liability on like domestic products, is inconsistent with the requirements of Article III:2, first sentence."[63]

The defeat of the Thai measure was predictable. The measure violated Article III:2, first sentence, because the automatic VAT exemption caused imported cigarettes to be subject to internal taxes in excess of those applied to like domestic cigarettes.

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60. *Id.* para. 116.

61. *Id.* para. 117 (quoting Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, para. 146, WT/DS161/AB/R, WT/DS169/AB/R (Dec. 11, 2000) (*adopted* Jan. 10, 2000)).

62. *See id.* para. 118.

63. *Id.*

4. GATT Article III:4: Potential Distortion of Conditions of Competition

Article III:4 states:

> The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded *treatment no less favourable* than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. The provisions of this paragraph shall not prevent the application of differential internal transportation charges, which are based exclusively on the economic operation of the means of transport and not on the nationality of the product.[64]

The Panel found that the Thai VAT measure also violates Article III:4. The Panel identified three aspects of the Thai VAT regime that result in extra administrative burdens on resellers of imported cigarettes. Specifically (as above), resellers of imported cigarettes: 1) must file monthly tax returns, 2) comply with "reporting and record-keeping requirements," and 3) are subject to penalties and sanctions for non-compliance.[65] Conversely, resellers of domestic cigarettes are exempt from these administrative requirements.

There are commonly three elements to an Article III:4 violation: likeness, measure, and discrimination. Only the third element was at issue on appeal: did Thailand violate the Article III:4 requirement concerning "treatment no less favourable"?[66] In its analysis concerning this element, the Panel took into account no less than four precedents, along with the market shares of imported and domestic cigarettes in Thailand, plus an econometric study submitted by the Philippines.[67] The Panel determined that the extra administrative burdens

64. General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, 1867 U.N.T.S. 187 (1994) [hereinafter GATT 1994] (emphasis added).

65. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 121.

66. That is, the threshold question in an Article III:4 dispute is, of course, whether the products are "like." The Appellate Body, borrowing Article III:4 language, said the second element requires that "the measure at issue constitute[] a law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution, or use of the products at issue." *Id.* para. 127.

67. *Id.* para. 131 (citing specifically as precedent Appellate Body Report, *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, WT/DS276/AB/R (Aug. 30, 2004) (*adopted* Sept. 27, 2004); Appellate Body Report, *United States – Section 211 Omnibus Appropriations Act of 1998*, WT/DS176/AB/R (Jan. 2, 2002) (*adopted* Feb. 1, 2002); Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R (Dec. 11, 2000) (*adopted* Jan. 10, 2001) [hereinafter Appellate Body Report, *Korea – Beef*]; and Report of the Panel, *United States – Measures Affecting Alcoholic and Malt Beverages*, at

imposed by the Thai measure on resellers of imported cigarettes "could potentially affect the *conditions of competition* for imported cigarettes in a negative manner."[68]

In so doing, the Panel adhered to Appellate Body jurisprudence to the effect that the test for whether treatment is unfavorable is whether that treatment tilts the competitive playing field, either actually or potentially. Thus, the Panel found that the measure granted favorable treatment to domestic cigarettes and violated Article III:4.[69]

On appeal, Thailand contended that "the Panel's analysis of 'treatment no less favourable' was insufficient as a matter of law to support a finding that Thailand acted inconsistently with Article III:4."[70]

206, DS23/R (Mar. 16, 1992) (*adopted* June 19, 1992) GATT B.I.S.D. (39th Supp.) (1992)).

68. *Id.* (emphasis added) (internal quotations omitted).

69. *See id.* para. 120.

70. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 122. Thailand made two additional arguments. First, Thailand accused the Panel of violating Article 11 of the DSU because the Panel accepted and relied on an exhibit submitted by the Philippines without affording Thailand an opportunity to comment on that evidence. *See id*. para. 141. The exhibit was submitted late in the proceedings and offered the expert opinion of a Thai tax lawyer on whether a reseller of domestic cigarettes must submit a monthly sales report. *See id*. para. 142. The Panel later used the exhibit to determine the measure constituted an extra additional duty imposed on imported cigarettes. *See id*. This finding helped lead the Panel to determine Thailand violated Article X:3. *See* para. 222. The Appellate Body noted that Thailand was not prevented from responding to the exhibit because it could have requested an opportunity to respond. *See id*. para. 160. The Appellate Body determined that the Panel had not erred in accepting and relying on the exhibit. *See id*.

The second Thai argument concerned GATT Article XX(d), the administrative necessity exception. The Panel held that "Thailand has not discharged its burden of showing that the administrative requirements and the imposition of penalties for failure to complete VAT filing requirements are necessary to secure compliance with the Thai VAT laws within the meaning of Article XX(d) of the GATT 1994." Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.758. Thailand appealed. Interestingly, Thailand did not "challenge the substance of the Panel's reasoning on Thailand's defense, as such." Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 164. Instead, Thailand argued that the Panel's express reliance on the findings of section VII.F.6(b)(ii) of that same report revealed "a fundamental error of legal analysis in its rejection of Thailand's defence under Article XX(d)." *Id*. (quoting Thailand's appellant's submission, which cited disapprovingly Panel Report, *Thailand – Cigarettes*, *supra* note 22, para. 7.758). This internal cross-reference in the Panel Report, Thailand claimed, resulted in a legal analysis error. *Id*. para. 167. The Philippines responded that the reference was merely a clerical mistake. *Id*. para. 168.

The Appellate Body agreed that the reference was an error, but it was unclear whether it indeed was a clerical mistake. Thus, the Appellate Body reversed the Panel's holding. *See id*. para. 171. Thailand also asked the Appellate Body, in the event of a reversal, to find that Thailand did not violate of Article III:4 "because the Panel 'effectively deprived Thailand of its right to assert its Article XX(d) defense' to that finding." *Id*. para. 172

Although Thailand acknowledged that administrative distinctions existed between imported and domestic cigarettes, it claimed the differences were "benign."[71] Thailand argued that treating imported cigarettes differently from domestic cigarettes does not translate ineluctably to less favorable treatment of imported cigarettes. The Panel, said Thailand, relied too heavily on "assertion" and "theoretical possibility."[72] Specifically, Thailand disputed the analysis by the Panel regarding "potentially" negative effects of the Thai measure on competition between imported cigarettes and domestic cigarettes.[73]

The Philippines countered with the correct argument that when imported products are subjected to a higher administrative burden than domestic products, as was the case here, the treatment is unequal and "'inherently less favorable' for imported goods."[74] According to the Philippines, the Panel "considered evidence of price elasticity and switching patterns and found that domestic and imported cigarettes operate in a close competitive relationship in the Thai market, such that the additional administrative requirements can potentially have a negative impact on the competitive position of imported cigarettes."[75] The Philippines noted that evaluating this evidence was above and beyond the analysis required by the Panel to establish its conclusion. Essentially, the Philippines used reasoning akin to that of the famous 1954 United States Supreme Court decision in *Brown v. Board of Education of Topeka*: racial segregation in education is inherently unequal, and differential administrative burdens are inherently unequal, too.

The Appellate Body offered observations on the well-established meaning of "treatment no less favourable" in Article III:4. Referring to its 2001 *EC – Asbestos* decision, the Appellate Body stated: "Where there is less favourable treatment of imported products, there is protection to domestic production."[76] According to the Appellate Body in its 2001 *Korea – Various Measures on Beef* ruling, the determination of less favourable treatment is marked

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(quoting Thailand's appellant's submission). The Appellate Body rejected this request by Thailand. *See id.* para. 173. Instead, the Appellate Body decided to review the record and rule on whether Thailand established an Article XX(d) defense. The Appellate Body noted that the Thai defense was quite short and contained "at least four critical flaws." *Id*. para. 178. In particular, the Appellate Body found the Thai argument regarding the element of necessity "patently underdeveloped." *Id*. para. 179. The Appellate Body determined, "Thailand failed to establish that its measure is justified under Article XX(d)." *Id*. para. 223(a)(ii).

71. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 132 (quoting Thailand's appellant's submission).

72. *Id.* para. 123 (quoting Thailand's appellant's submission).

73. *See id.* (quoting Thailand's appellant's submission).

74. *Id.* para. 124 (quoting Philippines' appellee's submission).

75. *Id.*

76. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 126. *See* Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, para. 100, WT/DS135/AB/R (Mar. 12, 2001) (*adopted* Apr. 5, 2001).

by "whether the measure at issue modifies the *conditions of competition* in the relevant market to the detriment of imported products."[77]

Relying on its *Korea – Beef* precedent, the Appellate Body said that regulatory differences between imported and domestic products are deemed a violation of Article III:4 if the differences result in a competitive advantage for the domestic product.[78] In other words, the mere existence of regulatory differences does not automatically trigger an Article III:4 violation. The complainant must also make a showing of competitive disadvantage to exports from its territory. In that sense, the Appellate Body did not accept the Philippine argument (and the suggested analogy to the *Brown v. Board of Education* decision).

The Appellate Body explained that an Article III:4 analysis of "less favourable treatment" must take into account the "fundamental thrust and effect of the measure itself."[79] That is, a proper analysis should include "the implications of the measure for the conditions of competition between imported and like domestic products."[80] The Appellate Body added that such an analysis neither necessitates nor precludes the use of empirical evidence.[81]

Based on its observations of Article III:4, the Appellate Body determined that the Panel sufficiently analyzed the Thai measure. The Appellate Body said the word choice of "potentially" and "potential effects" by the Panel merely references the reliance of the Panel on the 2000 *US – Foreign Sales Corporation* dispute.[82] According to the Appellate Body, the *Foreign Sales Corporation* case does not demand "inquir[ies] into the 'actual effects' of the additional administrative requirements."[83] The Appellate Body stated: "[I]t was reasonable for the Panel to conclude that compliance with the additional administrative requirements will involve some costs that resellers of imported cigarettes, and not resellers of like domestic cigarettes, must bear, taking account of, inter alia, economic evidence relating to the market."[84] According to the Appellate Body:

> [A]lthough the Panel could have inquired further into the implications of Thailand's measure for the conditions of competition, the mere fact that the additional administrative requirements are imposed on imported cigarettes, and not on like domestic cigarettes, provides, in itself, a significant

77. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 128 (quoting Appellate Body Report, *Korea – Beef*, *supra* note 67, para. 137 (emphasis in original)).

78. *See id.*

79. *Id.* para. 129 (quoting Appellate Body Report, *Korea – Beef*, *supra* note 67, para. 142 n.44).

80. *Id.*

81. *See id.*

82. *Id.* para. 135. *See* Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations,"* WT/DS108/AB/R (Feb. 24, 2000) (*adopted* Mar. 20, 2000).

83. Appellate Body Report, *Thailand – Cigarettes*, *supra* note 22, para. 135.

84. *Id.* para. 137.

> indication that the conditions of competition are adversely modified to the detriment of imported cigarettes.[85]

Thus, the Appellate Body upheld the Panel's holding and found Thailand in violation of Article III:4. It did so because the additional administrative burdens in the Thai measure on imported cigarettes treated those cigarettes less favorably than domestic cigarettes.[86] Put succinctly, the *Thai Cigarettes* case is another precedent for the proposition that a differential administrative burden that creates even a potential distortion of the conditions of competition between imported merchandise and the like domestic product violates GATT Article III:4 or, more generally, that the test for "treatment no less favourable" is an actual or potential tilt of the competitive playing field.

5. Commentary

a. Unfortunate Language

As noted above, in reaching its GATT Article III:4 holding, the Appellate Body stated that an Article III:4 analysis of "less favourable treatment" must take into account the "fundamental thrust and effect of the measure itself."[87] A careful edit of the Report should have resulted in this phrase being struck.

The phrase confuses the "treatment no less favourable test." The word "thrust" could intimate an inquiry into the intent behind the controversial measure, opening up questions of why a country took the measure it did and raising questions about proof techniques, such as the use of legislative history. The word "effect" could be read narrowly to mean only actual repercussions, excluding potential consequences. The Appellate Body would have done better to move right to its test (actual or potential conditions of competition) and eschew unnecessary, possibly confusing language.

b. Reference Pricing and Government Revenues

Why does the Thai government engage in reference pricing for cigarettes? The answer appears to be that it seeks to maximize its revenue from this product, which along with alcoholic beverages, typically is a large source of funds for developing countries. (Their use of the funds is not always corrupt. Thailand is committed to providing free or low cost HIV/AIDS medicines to poor people, and cigarette taxation not only is an attractive source of funds to provide the necessary pharmaceuticals, but also helps discourage smoking, which leads to

85. *Id.* para. 138.

86. *See id.* para. 140.

87. *Id.* para. 129 (quoting Appellate Body Report, *Korea – Beef*, *supra* note 67, para. 142 n.44).

other ailments.) Consider an extension of the above example of *X*, *Y*, and *Z* with respective VAT tax liabilities of $100, $400, and $500 based on the VAT formula of the difference between output and input taxes.

These tax liability figures imply market-based prices at each stage of $1,428.57 (in the initial transaction involving *X*), $5,714.29 (in the sale from *X* to *Y*), and $7,142.86 (in the same from *Y* to *Z*). The formula to determine these prices is:

$$7\% = \frac{\text{VAT Liability}}{\text{Market Price}}$$

With these prices, the Thai government would collect $1,000 of VAT revenue from the *X*-*Y*-*Z* transaction. (This figure is the sum of the respective VAT tax liabilities of $100, $400, and $500.) Suppose that government seeks to boost revenues to $1,200. It would set a reference price for each stage of the transaction of $400. Note that, at least on its face, the reference price scheme is not discriminatory because it applies both to TTM and foreign-made cigarettes. Hence, not surprisingly, the reference price scheme was not an issue at the Appellate Body stage of the case.

c. Unsurprising Results

The results of the *Thai Cigarettes* case are both straightforward and unsurprising. The Panel and Appellate Body closely adhered to precedent on GATT Article III. In the end, Thailand was unable to overcome the discriminatory effects on imported cigarettes that resulted from the VAT exemption for domestic cigarettes. Under the Thai VAT regime, imported cigarettes were subject to additional administrative burdens and, in some circumstances, VAT liability. The VAT exemption automatically and fully shielded domestic cigarettes from these burdens, thereby creating an unlevel playing field on which domestic cigarettes enjoyed a competitive advantage. The Appellate Body easily held that the Thai VAT exemption subjected imported cigarettes to less favorable treatment than domestic cigarettes because it imposed extra administrative burdens and, in some circumstances, a higher VAT than resellers of domestic cigarettes would ever encounter. Here, then, is another instance of the operation of de facto stare decisis in WTO adjudication.

B. Trade Remedies: Anti-Dumping

1. Citation

Appellate Body Report, *European Communities – Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China*, WT/DS397/AB/R (July 15, 2011) (*adopted* July 28, 2011).

2. Facts and Legal Background

In *EC – Fasteners*, while China raised many issues on appeal, the Appellate Body was presented with two basic issues vexing non-market economy (NME) exporting countries such as China: must an importing country imposing anti-dumping (AD) duties calculate the export price for each individual producer-exporter from the NME and likewise impose an individualized dumping margin on each particular respondent? Or does it suffice to use a countrywide dumping-margin calculation and anti-dumping duty rate? (The margin of dumping is determined by comparing the export price to the normal value; if the export price is lower, the difference is the margin.)

The European Union, in its regulations and in practice, had effectively presumed that Chinese importers were related to and effectively controlled by the Chinese government, with the result that they would all be treated as part of a single entity for export-price and dumping-margin purposes. The presumption was rebuttable; under certain circumstances (often met in practice), exporters could request and obtain "individual treatment," but the burden was on the exporters to demonstrate that they met the EU's criteria for such generally beneficial treatment.

Accordingly, *EC – Fasteners* concerns two AD measures of the EU, both of which China challenged.[88] The first measure, the European Union's Basic Anti-Dumping Regulation, bans dumped imports from non-EU countries[89] and is

88. Panel Report, *EC – Fasteners*, *supra* note 10. The Third Parties were Brazil, Canada, Chile, Colombia, India, Japan, Norway, Taiwan, Thailand, Turkey, and the United States. At the Panel stage, the respondent is referred to as the "European Communities" (EC). At the Appellate Body stage, the respondent is called the EU, given the name change from European Community to European Union via the Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community (Treaty of Lisbon), which was signed December 13, 2007, and entered into force December 1, 2009. The newer term is used herein.

89. *See id.* para. 2.1. The original measure China cited was Article 9(5) of Council Regulation (EC) No. 384/96 of Dec. 22, 1995. However, after the formation of the Panel, the EU repealed and replaced No. 384/96 with No. 1225/2009. The Chinese submissions are aimed at No. 1225/2009. *See* Council Regulation 1225/2009 on Protection Against Dumped Imports from Countries Not Members of the European Community, 2009 O.J. (L. 343) (EU) [hereinafter Basic AD Regulation], *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:343:0051:0073:EN:PDF.

generally referred to as the "Basic AD Regulation." The second challenged measure was a decision by the EU to impose an AD duty on certain Chinese iron or steel fasteners,[90] the "Definitive Regulation." In general, fasteners include screws and bolts, and are often used in automotive manufacturing, as well as other industries.[91]

China prevailed against the EU, as it did against the United States the same year in the *US – AD-CVD (China)* dispute. For China, and all NMEs, these victories were substantively significant in blunting the efforts of developed market economies to take remedial action against imports. Systemically, the wins were a signal that in the WTO system, at least the large and relatively wealthy emerging nations such as China, Brazil, and India enjoy the legal capacity to take action successfully against countries they viewed as the historically hegemonic trading nations.

Before the Panel, China argued that Article 9(5) of the Basic AD Regulation was inconsistent, "as such," with Article XVI:4 of the Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement), certain provisions of the Agreement on Implementation of Article VI of the GATT 1994 (AD Agreement), and Articles I:1, VI:1, and X:3(a) of GATT.[92] China also claimed the Basic AD Regulation violates certain articles of the AD Agreement "as applied" to the Definitive Regulation.[93]

As for the Definitive Regulation, China said that it violates certain provisions in the AD Agreement.[94] China challenged certain substantive aspects of the Definitive Regulation, including determinations by the EU on "standing, the definition of the domestic industry, the product under consideration, dumping and price undercutting, volume and impact of dumped imports, and causation."[95] China also challenged certain procedural aspects of the Definitive Regulation, including "disclosure . . . of information relevant to the investigation, the treatment of confidential information, and the procedural aspects of individual treatment claims."[96]

To understand the legal background to Basic AD Regulation Article 9(5), it is necessary to understand Article 2 of the Basic AD Regulation. In particular,

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90. *See* Panel Report, *EC – Fasteners*, *supra* note 10, para. 2.1. This decision by the EU is Council Regulation (EC) No. 91/2009 of Jan. 26, 2009.

91. *See* Daniel Pruzin, *Dumping: WTO Appellate Body Sides with China in Challenges to EU Dumping Rules*, 26 INT'L TRADE REP. (BNA) 1207 (July 21, 2011).

92. *See* Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumping Agreement), 1868 U.N.T.S. 201 (1994) [hereinafter AD Agreement]; Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 2. China challenged the Basic AD Regulation "as such" and "as applied" in the Definitive Regulation. Regarding the "as such" challenge, China cited violations of Articles 6:10, 9:2, 9:3, 9:4, and 18:4 of the AD Agreement. *Id.*

93. *See id.* Regarding the "as applied" challenge, China cited violations of Articles 6.10, 9.2, and 9.4 of the AD Agreement. *Id.*

94. *See id.* (putting Articles 2, 3, 4, 5, 6, and 12 of the AD Agreement at issue).

95. *See id.*

96. *Id.*

Article 2(7) sets out instances when a producer-exporter from a non-market economy country qualifies for market-economy treatment for the purpose of calculating the normal value.[97] Under Article 9(5), a producer-exporter from an NME country may be subject to a countrywide duty or may receive individual treatment.[98]

Article 2(1–7) of the Basic AD Regulation concerns the methodology for calculating the normal value.[99] Ordinarily, normal value is based on the price of the foreign like product in the home market of the respondent producer-exporter. In this case, that would mean the EU would consider sales of certain iron and steel fasteners in China.

Article 2(7) applies to NMEs. It divides NME countries into two categories: (i) NME countries that are WTO Members (plus Kazakhstan), and (ii) NME countries outside the WTO system.[100] The EU treats China as an NME, as do the United States and many other WTO Members, and puts it in the first category.

Article 2(7)(a) applies to non-WTO Member countries and requires the use of a proxy for the normal value when the subject merchandise originates in an NME.[101] The proxy may be:

1) Constructed value, based on costs of production (e.g., factor input prices) and other relevant figures from a market economy country;
2) Third-country price from a market economy country (i.e., the price of a like product sold in a third country that is a market economy, where "likeness" pertains to a comparison between (1) the product sold in that third country and (2) the subject merchandise (that is, the merchandise exported from the NME to the EU); or
3) The price at which the like product (i.e., a product that is like the subject merchandise exported from the NME to the EU) is sold from one market economy third country to another such country, including the EU.[102]

When it is impossible to use these proxies, Article 2(7)(a) permits the normal value proxy to be calculated by any other reasonable method.[103]

Note that the third proxy is perhaps a bit unusual because normal value and its proxies usually are based on data gathered entirely from outside the importing country that is taking action against subject merchandise. It is, however, logical. Using it, normal value would be based on sales from a third

97. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, paras. 273–274 (Article 2(8) and 2(9) concern the determination of the export price and its proxies.).
98. *See id.* para. 272.
99. *See id.* paras. 273–274.
100. *Id.* para. 273.
101. *See id.* para. 274.
102. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 274.
103. *Id.*

country (e.g., Thailand) either to another third country (e.g., India) or the EU itself. In the latter instance, that would mean the normal value is based on sales into the same country that is taking remedial action. But those sales are of a like product from a third country, not of subject merchandise from the respondent country. Might there be a relationship between the price data under the third proxy and the export (or constructed export) price of subject merchandise? For example, might the like product sales from a third country correlate with subject merchandise values? Possibly, but this matter was not at issue in the *EC – Fasteners* case.

Article 2(7)(b) is an important exception to Article 2(7)(a). Is it ever possible for a producer-exporter from an NME WTO Member to avoid having the normal value determined by a proxy? That is, is it possible to have a normal value based on foreign like product sales in that NME? Article 2(7)(b) responds "yes."

Article 2(7)(b) applies to Kazakhstan and any NME country that is a WTO Member at the time the EU launches an AD investigation.[104] Under Article 2(7)(b), a producer-exporter from one of these designated NME countries may use normal value instead of a proxy. But the producer-exporter must put forth sufficient evidence, subject to Article 2(7)(c), that "market economy conditions prevail" for the producer.[105] In turn, Article 2(7)(c) outlines the Market Economy Treatment (MET) test. The MET test contains criteria and procedures required to prove that a producer operates in market conditions.[106] If a producer can prove it operates in market conditions, it becomes subject to the criteria for determining a normal value under Article 2(1) to 2(6); i.e., the usual rules the EU applies to respondents from market economies.[107] If a producer-exporter fails to show it operates in market conditions, it becomes subject to Article 2(7)(a).[108]

Article 9(5) of the Basic AD Regulation outlines the procedure for applying an AD duty. It states:

> An anti-dumping duty shall be imposed in the appropriate amounts in each case, on a non-discriminatory basis on imports of a product from all sources found to be dumped and causing injury, except for imports from those sources from which undertakings [i.e., settlements of investigations, known as "suspension agreements" in American AD law] under the terms of this Regulation have been accepted.[109]

104. *Id.*
105. *Id.*
106. *See id.*
107. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 274.
108. *Id.*
109. Basic AD Regulation, *supra* note 89, art. 9(5).

Article 9(5) further requires the duty be specified "for each supplier or, if that is impracticable, and in general where Article 2(7)(a) applies, the supplying country concerned."[110]

In other words, an AD duty must be calculated for each respondent producer-exporter, unless one of the two stated exceptions applies: impracticability or an NME. If an exception applies, the AD determination necessarily must denote the countrywide duty, and there will be no individual, respondent-specific AD margins calculated or AD duties set. That is, the countrywide duty is the single AD rate applied to all imports and suppliers from the source country.[111]

To be sure, the EU provided an exception to the countrywide duty for certain NME suppliers. If an NME supplier can pass the individual treatment (IT) test, the EU designated it as an "IT supplier" and exempted it from the countrywide duty.[112] The Appellate Body summarized the IT test as requiring a respondent producer-exporter to meet all of the following stipulations:

> a) [No Capital Controls:] [I]n the case of wholly or partly foreign owned firms or joint ventures, exporters are free to repatriate capital and profits;
> b) [Free Market Pricing:] [E]xport Prices and quantities, and conditions and terms of sale are freely determined [i.e., not controlled by the government];
> c) [Private Ownership:] [T]he majority of the shares belong to private persons; state officials appearing on the board of directors or holding key management positions shall either be in the minority or it must be demonstrated that the company is nonetheless sufficiently independent from State interference;
> d) [Market Exchange Rates:] [E]xchange rate conversions are carried out at the market rate; and
> e) [Anti-Circumvention:] State interference is not such as to permit circumvention of measures if individual exporters are given different rates of duty.[113]

If a supplier does not meet every stipulation, it will remain subject to the countrywide duty. On the other hand, if a supplier passes the IT test, it qualifies for individual treatment and will receive an individual rate. The EU calculates the individual rate "by comparing the normal value from the market economy third country with the exporters' actual export prices."[114]

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110. *Id.*
111. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 275.
112. *Id.* para. 276.
113. *Id.*
114. *Id.* para. 277.

It may be helpful to reiterate which provisions of the Basic AD Regulation were *not* at issue before the Panel. China did not object to the MET test established in Article 2(7), nor did China challenge the use of normal value proxies based on market economy prices for imports from NME countries. Instead, according to the Appellate Body: "China directs its challenge to the rules regarding the specification of individual and country-wide duties for NME suppliers, including the IT test, which are contained in Article 9(5) of the Basic AD Regulation."[115]

Essentially, China railed successfully against the intransigence of the EU scheme. The mandate of Article 9(5) to apply a general, countrywide rate to NMEs was too strict, and the IT test did not loosen the rule. Here, then, was the essence of the dispute between China and the EU in the *Fasteners* case. China demanded individualized dumping margin and AD duty rate computations for at least some of its exporters and chafed at the EU imposing a single rate on all of them with no realistic opportunity for such exporters to achieve individual rates.

3. Key Issues on Appeal

The Panel held that Article 9(5) of the Basic AD Regulation violates "as such" Articles 6:10, 9:2, and 18:4 of the AD Agreement; Article I:1 of GATT; and Article XVI:4 of the WTO Agreement.[116] The EU contested these holdings, raising many arguments before the Appellate Body.[117] Distilling them to the key

115. *Id.* para. 282.

116. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, paras. 268–269.

117. *Id.* para. 270. As to the other less significant issues the EU raised on appeal, they and their resolutions were as follows:

- The EU claimed that Article 9(5) of the Basic AD Regulation is outside the scope of Article 6:10 because Article 9(5) does not concern dumping-margin determinations. The Appellate Body immediately dismissed the EU's claim that the scope of Article 9(5) is a matter of fact not subject to review. *See id.* para. 297. The Appellate Body upheld the finding by the Panel that Article 9(5) of the Basic AD Regulation concerns both the imposition of AD duties and calculation of the dumping margin. *See id.* para. 308.
- The Appellate Body said it was unnecessary to rule on an issue raised by the EU on appeal; namely, whether Article 9(5) of the Basic AD Regulation violated the MFN rule in GATT Article I:1 (and, in turn, whether the Panel violated Article 11 of the DSU). Essentially, the Panel held that Article 9(5) violates the MFN rule because it applies only to NME countries, not to all WTO Members. The Panel, however, did not spend much time on the matter. The Appellate Body recalled its earlier finding in which it upheld a Panel decision that Article 9(5) violates "as such" Articles 6:10 and 9:2 of the AD Agreement. Having established that violation, there was no need to ascertain whether an MFN violation also occurred. *See id*. para. 397. The Appellate Body also held that because Article 9(5) violates Articles 6:10 and 9:2 of the AD Agreement, the provision also runs afoul of Article XVI:4 of the WTO Agreement and Article 18:4 of the AD Agreement. *See id.* para. 401.
- The EU contended on appeal that the Panel erred in finding that the EU failed to provide, in a timely fashion, information to the Chinese suppliers that was important in the

points yields the following matters. That is, the case largely turned on these interpretative questions: first, does the AD Agreement (in Article 6:10) express a requirement, or merely an option, to calculate individual dumping margins for each respondent-producer exporter, whenever practical to do so? Second, does the Agreement (in Article 9:2) state a requirement, or just an option, to impose individual AD duties on each respondent-producer exporter, whenever practical to do so? China argued that the language in the relevant provisions was clear: there is a mandate, not a preference, for individualized calculations whenever practicable. So, on both points, China prevailed.[118]

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determination of the export price and normal value for the purposes of calculating the dumping margin, in violation of Article 6:2 of the AD Agreement. The Appellate Body upheld the decision of the Panel regarding the Article 6:2 violation by the EU. *See id.* para. 507. In doing so, the Appellate Body rejected the contention of the EU that the Panel decision was "purely consequential" and that the Panel had used Article 6:2 as a "catch-all provision." *Id*. paras. 506–507. The EU made a similar appeal under Article 6:4 of the AD Agreement. The Appellate Body did not rule on the EU appeal regarding an EU violation of Article 6:4 of the AD Agreement. *See id*. para. 505. The Appellate Body stated in dicta that the term "information" in Article 6:4 should be viewed broadly and that the information the EU withheld from the interested Chinese parties fell within the scope of that provision. *See id*. paras. 495, 505.

- Finally, the EU and China raised various contentions about the treatment of confidential information under Articles 6:2, 6:4, and 6:5 of the AD Agreement. The Appellate Body discussion of those matters is set forth in paragraphs 529 to 599 of its Report. Ultimately, the Appellate Body rejected these claims by China, largely on procedural grounds. *See id.* paras. 599, 624(d), 624(f).

118. While China prevailed on all significant substantive points before the Panel, the Appellate Body did disagree with a few of the Panel's relatively minor decisions:

- China claimed that the EU violated Articles 4:1 and 3:1 of the AD Agreement. In particular, China contested the EU's definition of the domestic industry, which the Panel accepted, in the dumping investigation of Chinese fasteners. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 410. China prevailed on its Article 4:1 appeal, but not on its Article 3:1 appeal. Regarding the alleged violation of Article 4:1, the Appellate Body recognized that when the industry is fragmented, as was the case here, the proportion of domestic production may be smaller than usually required. However, the Appellate Body determined that the EU had unnecessarily reduced the number of producer data that could contribute to a more accurate injury determination and "introduced a material risk of distorting the injury determination." *Id.* para. 430. Thus, the Appellate Body held that the EU failed to define the domestic industry consistently with Article 4:1 of the AD Agreement. Regarding the alleged violation of Article 3:1, the Appellate Body said that the EU, as the investigating authority, has discretion in how it identifies the sample. But the EU must follow two criteria: the domestic industry definition must comply with the AD Agreement, and the sample must "be properly representative of the domestic industry . . . ." *Id.* para. 436. The Appellate Body upheld the Panel decision but noted the narrowness of its holding. The holding, according to the Appellate Body, does not "address the issue of whether *the domestic industry defined by the Commission* in the fasteners investigation was consistent with this provision." *Id.* para. 438 (emphasis added).

Article 6:10 of the AD Agreement states:

> The authorities shall, as a rule, determine an individual margin of dumping for each known exporter or producer concerned of the product under investigation. In cases where the number of exporters, producers, importers or types of products involved is so large as to make such a determination impracticable, the authorities may limit their examination either to a reasonable number of interested parties or products by using samples which are statistically valid on the basis of information available to the authorities at the time of the selection, or to the largest percentage of the volume of the exports from the country in question which can reasonably be investigated.[119]

- The Appellate Body also reversed several other similar determinations by the Panel regarding Articles 3.1 and 4.1, while others were upheld. The Appellate Body found, for example, that the Panel had:

> [N]ot erred in its interpretation or application of Articles 4.1 and 3.1 of the *Anti-Dumping Agreement*, or acted inconsistently with Article 11 of the DSU, when finding that "the mere fact that the domestic industry as ultimately defined does not include any particular proportion of producers expressing different views with respect to the complaint, or producers who did not come forward within the 15-day period, does not demonstrate that the European Union acted inconsistently with Article 4.1 of the [*Anti-Dumping Agreement*] in defining the domestic industry" or acted inconsistently with Article 3.1 of that Agreement.

Id. para. 468 (quoting the Panel Report, *EC – Fasteners*, *supra* note 10, para. 7.219).

- China also challenged the holding by the Panel regarding the EU's Market Economy Treatment and/or Individual Treatment (MET/IT) claim forms. The Panel held that the EU was not in violation of Article 6:1:1 of the AD Agreement because the MET and/or IT claim forms are not subject to the thirty-day period referred to in Article 6:1:1. *See id.* para. 608. China challenged this holding on appeal, but lost. *See id.* paras. 623, 624(f). The issue hinged on whether the MET and/or IT claim forms were "questionnaires" within the meaning of Article 6:1:1. After a lengthy examination of the content and purpose of the MET and IT claim forms, the Appellate Body found that neither request of the Chinese exporters and producers would provide a substantial amount of information "upon which the Commission would base its determinations regarding the key aspects of an anti-dumping investigation." *Id.* para. 623. Upon finding that the forms fall outside the scope of Article 6:1:1, the Appellate Body upheld the Panel's holding. *See id.*
- China also argued that the EU violated Article 2:4 of the AD Agreement "by failing to make a 'fair comparison' between the Export Price and the Normal Value in the dumping determination" in the Definitive Regulation. *Id.* para. 469. The Appellate Body determined that the EU violated Article 2:4 by "failing to indicate to the parties in question what information was necessary to ensure a fair comparison." *Id.* para. 527.

119. *See* AD Agreement, *supra* note 92, art. 6:10.

In other words, an administering agency must compute a dumping margin for each individual producer-exporter, unless it is impracticable to do so, in which case, the agency must calculate margins for a reasonable number of producer-exporters and an all others rate (AOR) for the rest of them.

At issue on appeal was whether Article 9(5) of the Basic AD Regulation violates Article 6:10 of the AD Agreement "because it conditions the determination of individual dumping margins for producers or exporters from NMEs on the fulfillment of the individual treatment ('IT') test."[120] The IT test (as discussed above) contains five criteria (no capital controls, free market pricing, private ownership, market exchange rates, and anti-circumvention), all of which must be met if a respondent producer-exporter is to receive an individual dumping-margin calculation.

The EU argued unsuccessfully that Article 6:10 issues a preference, not a mandate, for calculating an individual dumping margin. Moreover, when dealing with NMEs, the IT test is capable of determining whether the government of an exporting country and individual producer-exporter effectively are a single entity for purposes of an AD investigation. China countered successfully that Article 6:10 compels investigators to calculate an individual dumping margin and that Article 9(5) of the Basic AD Regulation presumes, when dealing with NMEs, that a government and individual producers are a single entity. According to China, this presumption violates Articles 6:10 of the AD Agreement. Article 9:2 of the AD Agreement states:

> When an anti-dumping duty is imposed in respect of any product, such anti-dumping duty shall be collected in the appropriate amounts in each case, on a non-discriminatory basis on imports of such product from all sources found to be dumped and causing injury, except as to imports from those sources from which price undertakings under the terms of this *Agreement* have been accepted. The authorities shall name the supplier or suppliers of the product concerned. If, however, several suppliers from the same country are involved, and it is impracticable to name all these suppliers, the authorities may name the supplying country concerned. If several suppliers from more than one country are involved, the authorities may name either all the suppliers involved, or, if this is impracticable, all the supplying countries involved.[121]

At issue on appeal was whether Article 9(5) of the Basic AD Regulation violates Article 9:2 of the AD Agreement because it "conditions the imposition of individual duties on producers or exporters from NMEs on the fulfillment of the

120. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 270.
121. *See* AD Agreement, *supra* note 92, art. 9:2.

IT Test."[122] Manifestly, Article 9:2 is the cousin of Article 6:10. The latter provision explains when individual dumping-margin determinations should be made for each respondent producer-exporter. The former provision explains when individual AD duty rates should be imposed on each such respondent. Neither provision would be complete without the other, and the two together help ensure the AD scheme is logically tight in the sense that a particularized dumping-margin determination leads to a particularized AD duty.

Thus, unsurprisingly, the arguments on Article 9:2 from the parties were largely a rehash of their arguments regarding the alleged Article 6:10 violation. The EU argued that Article 9:2 states a preference, not a requirement, to collect individual AD duties and that the IT test legitimately determines whether a government and individual producer-exporters may be considered a single entity in an AD investigation. China countered that Article 9:2 imposes an obligation on investigators to issue individual AD duties and that the IT test violates Article 9:2 because it presumes a government and individual respondents from a NME are one. China argued that articles 6:10 and 9:2 do not impose on NME producer-exporters an obligation to overcome a presumption (such as the one in Article 9(5) of the EU Basic AD Regulation) that they are a single entity with their government.

In addition to its "as such" determination, the Panel held that the Basic AD Regulation "as applied" to the Definitive Regulation violated articles 6:10 and 9:2 of the AD Agreement.[123] So, on appeal, the EU requested the Appellate Body reverse this finding.[124] The Appellate Body declined to do so. Interestingly, in the underlying NME AD actions, the EU found that all the respondent producer-exporters passed the IT test. Hence, the EU argued, there was no actual violation in practice.

Yet, the Appellate Body observed that the IT test created a potential violation—and that was enough to constitute an illegality. Moreover, said the Appellate Body, the existence of the IT test could have discouraged producer-exporters from coming forward to seek an individual dumping margin or AD duty rate calculation. Therein was another potential violation. In brief, the Appellate Body rejected the EU argument that the way it applied the IT test in the underlying AD investigations did not affect the outcome of those cases. The EU ought to have known better than to make this argument. It is long-standing GATT-WTO jurisprudence that a violation need not actually manifest itself to be a violation. Even the potential for a violation is enough to make a disputed measure illegal.

Among various procedural issues, the only one of major significance was a Chinese challenge to the EU determination that that the EU's definition of the "domestic industry" as comprising only 25% of the total EU production of fasteners was inconsistent with Article 4.1 of the AD Agreement.[125]

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122. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 270.
123. *See id.* para. 400.
124. *Id.*
125. *Id.* para. 266(a)(i).

4. Principal Holdings and Rationale

a. Appellate Body Holding on "As Such" Violation of Basic AD Regulation Article 9(5)

The Panel (as mentioned) held that Article 9(5) of the Basic AD Regulation constitutes an "as such" violation of Articles 6:10, 9:2, and 18:4 of the AD Agreement; Article I:1 of GATT; and Article XVI:4 of the WTO Agreement.[126] The EU appealed these findings and lodged several arguments.

The EU argued on appeal that Article 9(5) of the Basic AD Regulation does not violate Articles 6:10 and 9:2 of the AD Agreement because the Panel erred in its interpretation of these two provisions.[127] The EU went on to contend that even if the Appellate Body agreed with the interpretation by the Panel, the Panel erred in its application of Articles 6:10 and 9:2 of the Agreement.[128] The Panel ultimately found that Article 9(5) of the Basic AD Regulation is inconsistent with Articles 6:10 and 9:2 of the Agreement because it requires the determination of countrywide dumping margins for, and the imposition of countrywide AD duties on, exporters or producers from NMEs, unless such producers or exporters show they are independent from their government under the EU IT test.[129]

The Appellate Body first examined the interpretation of Articles 6:10 and 9:2 of the AD Agreement and then went on to review their application by the Panel. Accordingly, there were three significant components to the Appellate Body decision concerning the "as such" violation created by Article 9(5).

b. Interpretation of Article 6:10 of the AD Agreement

The Appellate Body identified two issues of interpretation put forward by the EU on appeal. First, the EU claimed that Article 6:10 issues a preference, not an "unqualified obligation" for the calculation of an individual dumping margin.[130] According to the EU, "as a rule" means the obligation is not steadfast in "any and all circumstances."[131] By inserting "as a rule" after "shall," the drafters intentionally watered down the obligation, transforming it into merely a preference for calculating individual dumping margins over countrywide dumping margins. Put colloquially, the EU argument amounted to this: when a speaker says "as a rule," the listener hears two points: the rule, and then an exception to the rule; i.e., "as a rule" implies that the rule is not always followed.

126. *Id.* paras. 268–269.
127. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 270.
128. *See id.* para. 355.
129. *Id.* para. 310.
130 *Id.* para. 312.
131. *Id.*

China argued that the Uruguay Round negotiators intentionally inserted the verb "shall" into the AD Agreement and that it connotes a firm obligation.[132] According to China, "as a rule" links the obligation indicated by "shall," with the sole exception to the obligation, sampling, found in the second sentence of the same provision.[133]

Second, the EU claimed that the sampling exception in the second sentence of Article 6:10 is not the sole exception to "the rule."[134] In fact, there are other situations in which AD investigators need not calculate an individual dumping margin.[135] China rebutted this claim, too. China argued that the drafters would have explicitly stated any other exceptions they had in mind, as they did with the sampling exception.[136] But they did not do so; hence, the EU should not be allowed to invent one from whole cloth.

Given the two issues framed in the manner they were by the EU and China, a large swath of the Appellate Body Report predictably turned into a rather dull discussion of certain mechanics of the English language. The Appellate Body first reviewed whether Article 6:10 of the AD Agreement issues an obligation to calculate individual dumping margins. While "shall" normally is used to denote a requirement, here it is followed by "as a rule."[137] Per usual, the Appellate Body looked to the *Oxford English Dictionary* for guidance.[138] The Appellate Body observed that "as a rule" means "usually" and "more often than not."[139] The Appellate Body determined that "as a rule" modifies the obligation created by "shall," and thus limits the reach of the verb.[140] According to the Appellate Body, constructing the Article 6:10 language in this way ensures that it could be reconciled easily with other sections of the AD Agreement with which it might otherwise conflict.[141]

But, said the Appellate Body, this flexibility was not so great as to favor the EU. The Appellate Body stressed that the deliberate use of "shall" demonstrates the drafters intended Article 6:10 to express more than a preference.[142] In contrast, by transforming the clause into a preference, the EU stripped "shall" of its ordinary meaning.[143]

The Appellate Body's second interpretation concerned the explicit exception found in Article 6:10, second sentence, to the requirement of Article 6:10, first sentence. On this rather modest point, the Appellate Body held in favor

132. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 313.
133. *Id.*
134. *Id.* para. 312.
135. *See id.*
136. *Id.* para. 313.
137. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 316.
138. *Id.*
139. *Id.* (citing 1 SHORTER OXFORD ENGLISH DICTIONARY (6th ed. 2007)).
140. *Id.* para. 317.
141. *Id.*
142. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 316.
143. *See id.* para. 317.

of the EU. The Appellate Body noted that several instances (not involving sampling) within the AD Agreement exist that constitute explicit exceptions to the Article 6:10 obligation.[144] In one such exception, Article 9:5 provides that when "new exporters cannot show that they are not related to any of the exporters or producers that are subject to the anti-dumping duties," the calculation of an individual dumping margin is not required; i.e., this exception is for so-called new shippers.[145] The Appellate Body observed that "as a rule" in Article 6:10, first sentence, "anticipates the exception that follows in the second sentence of Article 6:10." But "as a rule" also anticipates exceptions in other sections of the AD Agreement.[146]

The Appellate Body cautioned that its interpretation does not allow WTO Members to "create exceptions, which would erode the obligatory character of Article 6:10."[147] The Appellate Body summarized its holding on each of the aforementioned issues:

> [W]e interpret Article 6:10 of the *Anti-Dumping Agreement* as *expressing an obligation, rather than a preference, for authorities to determine individual margins of dumping*. This obligation is qualified and is subject not only to the exception specified for sampling in the second sentence of Article 6.10, but also to other exceptions to the rule to determine individual dumping margins that are provided for in the covered agreements.[148]

In other words, the obligation to calculate individual dumping margins prevails to the point it is consistent with the other provisions in the covered agreements.[149]

c. Interpretation of Article 9:2 of the AD Agreement

According to the Panel's interpretation, Article 9:2 of the AD Agreement permits authorities to name the supplying country, instead of individual exporters or producers, when there are so many producer-exporters that it is "impracticable"

144. *Id.* para. 319.

145. *Id.*

146. *Id.* para. 320.

147. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 320.

148. *Id.* para. 329 (emphasis added).

149. The EU also put forth five exceptions to the rule in Article 6.10 of the AD Agreement. *See id.* paras. 321–326. The Appellate Body examined these exceptions after its analysis of Article 6:10 and determined that the examples "are consistent with the binding nature of the rule set forth in the first sentence of Article 6.10 and, therefore, do not support the European Union's claim that Article 6.10 states a mere preference." *Id.* para. 327.

to list each one.[150] However, the Panel noted that Article 9:2 "does not . . . allow the imposition of a single country-wide anti-dumping duty in an investigation involving [an NME]."[151]

On appeal, the EU made an argument similar to its argument regarding Article 6:10. So, again, the Appellate Body dealt with two main interpretive questions: first, what exactly do the first two sentences of Article 9:2 require investigators to do? On the one hand, do those provisions merely require an administering authority to identify the names of individual producer-exporters, but leave the investigators with the discretion to impose on them a countrywide (or AOR) AD rate? Or, on the other hand, do those provisions mandate the authority to both identify individual producer-exporters and impose on them individual AD duties (which, of course, would be based on individualized dumping-margin calculations under Article 6:10)? Second, does the impracticability exception in Article 9:2 apply to situations other than sampling "where it would not be 'effective' to impose individual duties in respect of NMEs?"[152]

In effect, the Article 9:2 issues were the logical extension of the Article 6:10 issues: the latter concerned individual dumping-margin calculations, while the former concerned the imposition of individual dumping duties. Logically then, the Article 9:2 result followed from the Article 6:10 result. The Appellate Body held that Article 6:10 mandates individual dumping-margin calculations, even in the NME context, albeit with more exceptions than just sampling. So the Appellate Body had to hold that Article 9:2 mandates the imposition of individualized AD duty rates to NME producer-exporters, albeit with more exception than just sampling. If the Appellate Body had held differently, it would have flunked an elementary test concerning logical implication.

First, the EU asserted that Article 9:2 contains a preference, not a requirement, for imposing individual AD duties.[153] The EU said the only obligation of Article 9:2 is to identify suppliers of subject merchandise.[154] According to the EU, Article 9:2 "reflects a product-wide and country-wide approach in that it refers to the imposition of an anti-dumping duty on a 'product,' not a company."[155] China countered: "[T]he fact that Article 9.2, first sentence, refers to the imposition of anti-dumping duties with respect to a 'product' does not entail an authorization to impose country-wide duties."[156] In other words, China argued that 9:2 compels investigators to impose individual AD duties, with the exception of the situation listed in Article 9:2, third sentence.[157]

Second, the EU argued that Article 9(5) of the Basic AD Regulation falls within the scope of the exception in Article 9:2 of the AD Agreement. The EU

150. *Id.* para. 330.
151. *Id.* (quoting the Panel Report, *EC – Fasteners*, *supra* note 10, para. 7.112).
152. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 330, para. 331.
153. *Id.* para. 333.
154. *Id.* para. 337.
155. *Id.* para. 333.
156. *Id.* para. 334.
157. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 334.

claimed that Article 9:2 allows countrywide duties to be imposed not only under the sampling exception, but also when it is "impracticable" to impose individual duties.[158] China largely agreed with the decision of the Panel but stipulated that Article 9:2, third sentence, does not permit "the imposition of a country-wide duty in the case of imports from NMEs."[159]

Regarding the first interpretive issue, the Appellate Body observed the use of "shall" in the first and second sentences of Article 9:2 means it is mandatory for the authorities to list suppliers of subject merchandise and collect the appropriate AD duties.[160] The Appellate Body contrasted the mandatory nature of the first two sentences of Article 9:2 with the second sentence of Article 9:1. Article 9:1, second sentence, states that "it is desirable" to impose AD duties in amounts less than the dumping margin if they will reasonably address the injury to the domestic industry.[161] (That sentence justifies the "Lesser Duty Rule" in EU AD law.) The phrase "it is desirable" designates a preference, while the word "shall" designates a mandatory rule.[162]

Furthermore, said the Appellate Body, the word "sources" designates individual suppliers and not the "country as a whole."[163] Thus "the requirement under Article 9.2 that anti-dumping duties be collected in appropriate amounts in each case and from all sources relates to the individual exporters or producers subject to the investigation."[164]

The Appellate Body reasoned that because Article 6:10 requires determination of individual dumping margins, then it naturally follows that Article 9:2 refers to the imposition of an individual AD duty.[165] In other words, the "appropriate amount" of duty to be collected is an individual duty.[166]

The Appellate Body also determined that Article 9:2, second sentence, requires an administering authority to list the suppliers of the subject merchandise.[167] The suppliers that must be listed are those from which individual AD duties are to be collected.[168] The Appellate Body noted that this view is corroborated by the entire context of Article 9 of the AD Agreement.[169]

Regarding the second interpretive issue, the Appellate Body reiterated that the exception in Article 9:2, third sentence, permits "importing Members to specify duties for the supplying country concerned, where specification of

158. *Id.* para. 343.
159. *Id.*
160. *Id.* para. 336.
161. *Id.*
162. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 316.
163. *Id.* para. 338.
164. *Id.*
165. *Id.* para. 339.
166. *Id.*
167. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 340.
168. *Id.*
169. *Id.* para. 341.

individual suppliers is 'impracticable.'"[170] The Appellate Body declined to define the exact scope of the exception, but instead narrowly examined whether Article 9(5) of the Basic AD Regulation fit within the stated exception. Specifically, the Appellate Body examined "whether it can be considered 'impracticable' to impose individual anti-dumping duties on suppliers from NMEs that do not meet the IT test."[171]

Pulling out, once more, the *Oxford English Dictionary*, the Appellate Body reprinted the definition of "impracticable": "not practicable; unable to be carried out or done; impossible in practice."[172] The EU, said the Appellate Body, mistakenly interprets the Article 9:2 exception as relating to ineffectiveness, as opposed to impracticability.[173] The Appellate Body determined the exception for listing the supplying country when listing the individual supplier does not extend to the EU in the *Fasteners* case.[174] Thus, the imposition of countrywide duties on non-IT suppliers from NMEs under Article 9(5) of the Basic AD Regulation does not fall within the scope of exception in Article 9:2 of the AD Agreement.[175]

In sum, the Appellate Body held that Article 9:2, first and second sentences, require an administering authority "to specify an individual duty for each supplier, except where this is impracticable, when several suppliers are involved."[176] The Appellate Body also held that the exception in Article 9:2, third sentence, does not allow a countrywide duty to be levied when it would be merely ineffective to impose an individual duty.[177] Rather, the imposition of an individual duty must prove impracticable to justify resorting to an AOR.[178]

d. Application of Articles 6:10 and 9:2 of the AD Agreement

The EU argued that even if the Appellate Body accepted the interpretation by the Panel of Articles 6:10 and 9:2 of the AD Agreement, the Panel erred in the application of those provisions. In particular, the EU asserted that when dealing with NMEs, a supplier and the government of the supplier may be considered a single exporter or producer for the purposes of an AD investigation.[179] Furthermore, argued the EU, the IT test is a sufficient tool for

170. *Id.* para. 342.
171. *Id.* para. 345.
172. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 347.
173. *See id.* para. 348.
174. *Id.* para. 351.
175. *See id.*
176. *Id.* para. 354.
177. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 354.
178. *Id.*
179. *Id.* para. 369; *see id.* paras. 346, 348, 352. Note that the EU made a second argument regarding the application of Articles 6:10 and 9:2 of the AD Agreement. The EU claimed that AD investigators may presume all suppliers in NMEs are associated with the government. *See id*. para. 357. The EU argued that the Panel violated Article 11 of the DSU because "it disregarded evidence submitted by the European Union relating to such a

determining whether the government and an exporter-producer may be deemed a single entity.

First, the Appellate Body reviewed the analysis of the Panel. Relying on the 2005 *Korea – Certain Paper* case, the Panel determined that Article 6:10 of the AD Agreement allows AD investigators to treat several "legally distinct entities" as a single exporter or producer as long as there is a sufficiently close structural and commercial relationship between the entities.[180] However, the Panel took care to distinguish the present fasteners case from *Korea – Certain Paper*. According to the Panel, the IT test in Article 9(5) of the Basic AD Regulation fails to sufficiently address the structural and commercial relationship between the government and exporters in NMEs. Instead, said the Panel, the IT test addresses "the role of the State in the way business is conducted in a given country."[181] So, the Panel reasoned, the government becomes akin to the "'parent company' for potentially thousands of distinct legal entities producing and exporting a product under investigation."[182] According to the Panel, this approach by the EU is inconsistent with *Korea – Certain Paper*.[183]

First, the Appellate Body looked at whether the government of a producer-exporter and individual producer-exporters could constitute a single entity in an AD investigation. The Appellate Body said *Korea – Certain Paper* "considered that there may be situations where several closely related suppliers may be deemed a single supplier for the purposes of Article 6.10 and referred to a 'structural and commercial relationship.'"[184] This interpretation did not alter the previously accepted significance of "each known exporter or producer" or the exceptions to Article 6:10 of the AD Agreement.[185] The Appellate Body noted that the *Korea – Certain Paper* case does not expressly sort out whether producer-exporters and the government of the producer-exporters could constitute a single entity.[186]

The Appellate Body, for the purpose of an AD investigation, ruled that Articles 6:10 and 9:2 of the AD Agreement "do not preclude" a government and individual producer-exporters from constituting a single entity.[187] The Appellate Body gave several examples of when the calculation of a single dumping margin

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presumption." *Id.* The Appellate Body held that the Panel did not violate Article 11 of the DSU because the evidence the EU submitted was irrelevant. The Appellate Body said that the EU failed to establish that the "economic structure in China justifies a general presumption that the State and all the exporters in all industries that might be subject to an anti-dumping investigation constitute a single legal entity." *Id*. para. 369.

180. *See id*. para. 371; *see also* Panel Report, *Korea – Anti-Dumping Duties on Imports of Certain Paper from Indonesia*, WT/DS312/R (Oct. 28, 2005) (*adopted* Nov. 28, 2005).

181. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 372.

182. *Id.*

183. *Id.*

184. *Id.* para. 374.

185. *Id.*

186. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 380.

187. *Id.* para. 376.

for multiple suppliers may be valid under Article 6:10 of the AD Agreement.[188] Some acceptable situations include common shareholders or management between suppliers (or between suppliers and the government of the suppliers), or government-controlled prices or output.[189]

Next, the Appellate Body checked to see whether the IT test is an appropriate tool to determine whether a government and individual producer-exporters could constitute a single entity. According to the Appellate Body, the purpose of the IT test is to determine whether exporters deserve individual treatment under Article 9(5) of the Basic AD Regulation.[190] Although the IT test shows how independent of one another the producer-exporters are, some of the elements of the test can illuminate linkages between or among them.[191] The Appellate Body observed:

> [B]y focusing on State interference with exporters and State intervention in the economy in general, the IT test captures broader market distortions in the economy and different kinds of interferences by the State than that of the control or material influence by the State over the exporters in respect of pricing and output of a particular like product.[192]

Therefore, said the Appellate Body, the IT test can prevent an exporter from gaining individual treatment even when the relationship between the government of the exporter and individual exporter does not merit treatment as a single exporter under Articles 6:10 and 9:2 of the AD Agreement.[193] In the end, the Appellate Body agreed with the Panel: the purpose of the IT test is not to determine whether legally distinct entities can constitute a single exporter or producer.[194]

The Appellate Body noted that while the IT test was not helpful in determining whether suppliers of subject merchandise and the government of those suppliers could constitute a single entity, the criteria used in *Korea – Certain Paper* are relevant, if not all-inclusive.[195] For example, the Appellate Body said that examining corporate links would help determine whether the exporters and the government are sufficiently connected as to constitute a single entity under Articles 6:10 and 9:2 of the AD Agreement.[196] The Appellate Body observed that in some circumstances, a government and private exporters may be considered a single entity under Articles 6:10 and 9:2 of the Agreement if the

188. *Id.*
189. *Id.*
190. *See id.* para. 377.
191. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 377.
192. *Id.* para. 379.
193. *Id.*
194. *Id.* para. 377.
195. *See id.* para. 380.
196. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 381.

government of a respondent exercises sufficient "control or material influence in and coordination of these exporters' pricing and output."[197] However, the Appellate Body reiterated, the IT test cannot make such a determination.[198] The Appellate Body noted:

> [E]ven where it could be determined that particular exporters that are related constitute a single supplier, Articles 6.10 and 9.2 of the *Anti-Dumping Agreement* would nonetheless require the determination of an individual dumping margin for the single entity, which should be based on the average export prices of each individual exporter, and the imposition of a corresponding single anti-dumping duty.[199]

The Appellate Body also clarified that the dumping margin must be "based on a weighted average of export prices of each individual exporter" in the single entity in order to comply with Article 6:10 of the AD Agreement.[200]

In the end, the Appellate Body upheld the findings of the Panel. The Appellate Body held that Article 9(5) of the Basic AD Regulation violates the "as such" Articles 6:10 and 9:2 of the AD Agreement because it "conditions the determination of individual dumping margins for and the imposition of individual anti-dumping duties on NME exporters or producers" on the IT test.[201]

e. Appellate Body Holding on "As Applied" Violation of Basic AD Regulation Article 9(5)

On appeal, the EU also contended that Article 9(5) of the Basic AD Regulation "as applied" in the AD investigation underlying the *Fasteners* case did not violate Articles 6:10 and 9:2 of the AD Agreement. The Appellate Body said that even though all the suppliers met the IT test in the investigation, Article 9(5) "as applied" still may be deemed to violate the Agreement.[202] The Appellate Body stated that "[t]he very existence of the IT Test" hurt Chinese exporters in the fasteners case because they had to prove they should receive individual treatment.[203] The AD Agreement does not contain a presumption the Chinese exporters had to overcome.[204] So the Appellate Body upheld the decision of the

197. *Id.* para. 382.
198. *Id.*
199. *Id.* para. 383.
200. *Id.* para. 384.
201. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 385.
202. *Id.* para. 407.
203. *Id.* para. 408.
204. *Id.*

Panel and ruled that Article 9(5) of the Basic AD Regulation violates Articles 6:10 and 9:2 of the AD Agreement "as applied" in the Definitive Regulation.[205]

f. Definition of "Domestic Industry" Under Articles 3.1 and 4.1, AD Agreement

China had argued before the Panel that the domestic industry as defined by the EU in the investigation did not include producers whose output collectively "constitutes a major proportion of total domestic production" under Article 4.1 of the AD Agreement. China also argued that the EU injury definition was based on an unrepresentative sample of the industry.[206] The Appellate Body suggested that a "major proportion" ought to be "determined so as to ensure that the domestic industry defined on this basis is capable of providing ample data that ensure an accurate injury analysis."[207] Further, the investigating authority, so as to assure the accuracy of the injury determination, "must not act so as to give rise to a material risk of distortion in defining the domestic industry, for example, by excluding a whole category of like product."[208] Also, the higher proportion of total domestic production that is considered, the less likely that injury determinations would be distorted.

The EU had argued that it was permissible under the AD Agreement to treat 25% or more of domestic production as legitimately representing a major proportion of domestic production.[209] The Appellate Body disagreed, noting the absence of a "technical basis" for that supposition and observing that the 25%/50% requirements[210] for initiating an investigation serve a different purpose. This benchmark, under Article 5.4 of the AD Agreement, "does not address the question of how the entire universe of the domestic industry *itself* should be defined."[211] Ultimately, the AD Agreement negotiations did not define a "major

205. *Id.* para. 409.

206. *See* Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 410.

207. *Id.* para. 413.

208. *Id.* para. 414.

209. *Id.* para. 418 (referring to the AD Agreement, art. 5.4) (citing the EU's appellee's submission).

210. *See* AD Agreement, *supra* note 92, art. 5.4 ("An investigation shall not be initiated pursuant to paragraph 1 unless the authorities have determined, on the basis of an examination of the degree of support for, or opposition to, the application expressed by domestic producers of the like product, that the application has been made by or on behalf of the domestic industry. The application shall be considered to have been made 'by or on behalf of the domestic industry' if it is supported by those domestic producers whose collective output constitutes more than 50 per cent of the total production of the like product produced by that portion of the domestic industry expressing either support for or opposition to the application. However, no investigation shall be initiated when domestic producers expressly supporting the application account for less than 25 per cent of total production of the like product produced by the domestic industry.").

211. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 418.

proportion."[212] Therefore, the term requires that "the domestic industry defined on this basis encompass producers whose collective output represents a relatively high proportion that substantially reflects the total domestic production."[213] In order for the authority to meet the "major proportion" requirements in the case of a less fragmented industry than the EU fastener industry, the industry must be defined in such a way as to avoid a "material risk of distortion."[214]

The EU had argued that 27% of domestic production was considered satisfactory under the EU Basic AD regulation, Articles 4(1) and 5(4).[215] Among the justifications offered was the fact that the sample size was limited by the fact that twenty-five out of 318 producers surveyed were unwilling to participate in the authority's sample. For the Appellate Body, the unwillingness of twenty-five producers to be included was not a valid excuse for limiting the evaluation of domestic producers to only 27% of domestic production.[216] In any event, the 25% benchmark used by the EU did not address the standard of a "major proportion" and so did not meet the requirements of Article 4.1 of the AD Agreement, and the Panel was wrong to conclude otherwise.[217]

China had also argued that the EU actions were inconsistent with Article 3.1 of the AD Agreement because the sample was not representative of the domestic industry, in part because the sample was not selected in a statistically valid manner.[218] The Appellate Body largely rejected this criticism on grounds that Article 3.1 neither provides for sampling nor indicates how any sampling used should be undertaken.[219] Nor does the AD Agreement require the investigating authority (in this case, the EU Commission) to analyze microeconomic injury factors as part of its determination.[220] Ultimately, the Appellate Body rejected most other challenges to the manner in which the Commission put together the listing of domestic producers who produced data used in the injury finding, including the exclusion of producers that did not support the complaint or respond to the Commission's questionnaire in a timely manner.[221]

212. *Id.*
213. *Id.* para. 419.
214. *Id.*
215. *Id.* paras. 423, 428.
216. Appellate Body Report, *EC – Fasteners*, *supra* note 10, para. 429.
217. *Id.* paras. 429–430.
218. *Id.* para. 431.
219. *Id.* paras. 435–436.
220. *Id.* paras. 437–438.
221. Appellate Body Report, *EC – Fasteners*, *supra* note 10, paras. 439–468.

g. The Principal Holding on Individualized Calculation of Export Price

In sum, the 2011 *EC – Fasteners* case stands for the proposition that Articles 6:10 and 9:2 of the AD Agreement do not countenance application of a countrywide dumping margin and AD duty determination to respondent producer-exporters from NMEs. Rather, NME AD rules must be flexible enough to allow for individualized calculations. This proposition rests on the interpretation of Articles 6:10 and 9:2; namely, the key language in them, respectively, that investigating authorities *must* calculate individual dumping margins and *must* collect individual duties. Article 9(5) of the Basic AD Regulation violated Articles 6:10 and 9:2 of the AD Agreement because it presumed, in NMEs, that the government of an exporting country and individual producer-exporters from that country are a single entity for the purposes of calculating dumping margins and AD duties.

This case marks one of several cases in the latter part of the first decade of Chinese membership in the WTO in which China prevailed at the Appellate Body level. Put bluntly, the case shows how quickly the People's Republic has emerged as an effective advocate for its global trade interests, even against traditional hegemonic trading powers like the EU (and the United States, as in *US – AD/CVD (China)*, discussed in Part II.D.). These wins are a result of the increased sophistication and aptitude within the Chinese legal profession. The successes are evidence in favor of the consensus that China is a major trading power with a voice not to be ignored.

5. Commentary

a. Increasing the Burden on the Investigating Authority

As in *US – AD/CVD (China)*, the most significant effects of the Appellate Body ruling in *EC – Fasteners* are less likely to be lower dumping margins than an increase in the volume of factual information the investigating authority will be required to gather to meet its burden of proof in the event that the authority decides to treat certain exporters as a single entity for purposes of calculating dumping margins. As a result, questionnaires sent by the authority to individual exporters are likely to increase in length and complexity, and the risks of the authority's use only of those "facts available" (in reliance on AD Agreement Article 6.8) if the enterprises fail to provide full information in a timely manner are magnified, adding to the cost and complexities of legal representation. While questionnaires from the investigating authority typically are not sent to the government in anti-dumping cases (as distinct from those relating to countervailing duties), it is conceivable that this practice could change, as the authority will effectively be required to demonstrate in many instances that the relationship of the exporters to the government justifies their treatment as a single

entity.[222] Still, there will likely be more situations in EU investigations, as with those concluded in the United States, where producer-exporters will receive individual rather than countrywide export prices and the resulting dumping margins.

It may well be that the United States government has already recognized this additional burden. Under President Obama's fiscal year 2013 budget proposal, $26 million was requested for the new Interagency International Trade Enforcement Center. Most of that amount, $24 million, would go to the Department of Commerce's International Trade Administration, which is responsible for, inter alia, the Office of Import Administration, the investigating authority for anti-dumping and CVD cases.[223]

b. Similar Questions in U.S. NME Anti-Dumping Practice: Separate Rates[224]

Although the term "individual treatment" is not used in U.S. anti-dumping law, there are strong similarities to EU regulations and practice. The presumptive approach for NME producers in the Department of Commerce's AD investigations is to apply a countrywide dumping margin to all of them on the ground that all are government-controlled. However, if an NME producer can demonstrate that it is *not* government-controlled, both as a matter of law and in practice, the Department of Commerce (DOC) will apply a separate, individual rate in determining that producer's export price.[225] (Separate rates do not apply to the determination of a normal value, to which export price is compared to determine whether there are dumped sales; i.e., sales in the export market at less than the normal value.)

The DOC has developed a "separate rates" test for determining when such individual treatment is warranted.[226] This test focuses on whether the company is

222. *See id.* para. 374.

223. *Under Proposal for Enforcement Center, ITA Would Get Most New Funds*, WORLD TRADE ONLINE, Feb. 16, 2012, http://insidetrade.com/Inside-US-Trade/Inside-U.S.-Trade-02/17/2012/under-proposal-for-enforcement-center-ita-would-get-most-new-funds/menu-id-710.html.

224. This section is adapted in part from David A. Gantz, *Polyethylene Retail Carrier Bags: Non-Market Economy Status and U.S. Unfair Trade Actions against Vietnam*, 36 N.C. J. INT'L L. & COM. REG. 85 (2010) [hereinafter Gantz, PRCBs].

225. U.S. DEP'T OF COMMERCE, 2009 ANTIDUMPING MANUAL ch. 10, 3 (2009) *available at* http://ia.ita.doc.gov/admanual/index.html (Market oriented industry treatment is codified in neither U.S. statutes nor U.S. regulations, so its legal status is somewhat unclear from the U.S. domestic law point of view.).

226. Antidumping Methodologies in Proceedings Involving Non-Market Economy Countries: Surrogate Country Selection and Separate Rates, 72 Fed. Reg. 13,246, 13,247–48 (Mar. 21, 2007) [hereinafter Surrogate Country Selection]; Notice of Final Determination of Sales at Less Than Fair Value: Bicycles from the People's Republic of China, 61 Fed. Reg. 19,026, 19,027 (Apr. 30, 1996).

a de jure or de facto government-controlled entity. A lack of de jure governmental control is indicated by: a) an absence of restrictions on its business operations and exports; b) any governmental legislation that illustrates a lack of governmental control (for example, privatization legislation); and c) other governmental actions that indicate that the company is not controlled by the government.[227] Whether the NME government exercises de facto control is indicated by: a) whether the company's export prices are set by the government, b) whether the company is free to negotiate and sign contracts without government involvement or approval, c) whether the company may make autonomous decisions with regard to management selection, and d) whether the company retains its export sales revenue and makes its own decisions regarding how to use its profits or finance its losses.[228] The onus is on the producer-exporter to seek separate rate status; otherwise, the DOC will apply a countrywide rate.

Thus, while the structure of the separate rate test used by the DOC is somewhat different from the approach contained in EU regulations (and found wanting by the Appellate Body), the presumption is against the use of separate rates and the burden of proof under current DOC practice is on the exporters rather than on the investigating authority. As with the EU, the DOC, in practice, has frequently granted separate-rate status to exporters that applied for it.[229]

c. Compliance

The European Union initially advised the Dispute Settlement Body (DSB), on August 18, 2011, that it intended to implement the rulings and recommendations of the DSB consistently with its WTO obligations. In January 2012, the EU reported that it had agreed with China that the "reasonable period of time" for implementation would be approximately fourteen months, which expired on October 12, 2012.[230]

227. Surrogate Country Selection, *supra* note 226, at 13,248.

228. *Id*.

229. *See, e.g.*, Gantz, PCRBs, *supra* note 224, at 121–22.

230. *See* WTO Secretariat, *European Communities – Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China: Summary of the Dispute to Date*, Feb. 16, 2012, *available at* http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds397_e.htm.

C. Trade Remedies: Countervailing Duties

1. Citation

Appellate Body Report, *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft*, WT/DS316/AB/R (May 18, 2011) (*adopted* June 1, 2011) (complaint by the United States).[231]

2. Background[232]

a. Lengthy, Tortuous Reading

In the *Airbus* case, WTO adjudicators managed to break their own ignominious record for issuing the longest reports. The *Airbus* Panel Report numbers 1,049 pages and 6,083 footnotes. The Appellate Body slimmed those figures down to 613 pages and 3,068 footnotes. (Mind you, these figures are with Business Confidential Information (BCI) deleted from both reports and exclude their Annexes.) The previous Panel Report record seems to have been set in the *Genetically Modified Organisms* case,[233] while the previous Appellate Body Report record appears to have been in the *Cotton* case.[234] To be sure, more is coming: the Panel Report in the EU complaint against the United States for alleged subsidies to Boeing is a hefty 783 pages (again, without BCI or

231. Appellate Body Report, *EC – Airbus*, *supra* note 8; see also Panel Report, *EC – Airbus*, *supra* note 8. The complainant was the United States, and Australia, Brazil, Canada, China, Japan, and Korea were third parties in both the Panel and the Appellate Body proceedings.

As with *EC – Fasteners*, the term "European Union" replaced "European Community" during the proceedings. *See* note 88. As the Appellate Body explained, the case began on July 20, 2005, with the establishment of a Panel before the name-changing Treaty of Lisbon entered into force on December 13, 2007. Throughout their reports, however, the Panel and the Appellate Body reference the European Union, but regrettably from the vantage point of simplicity, the Appellate Body chose not to adhere to a standardized reference.

232. This discussion is drawn from the WTO dispute settlement case file DS316, *European Communities – Measures Affecting Trade in Large Civil Aircraft*, *available at* http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds316_e.htm [hereinafter WTO DS316]; Appellate Body Report, *EC – Airbus*, *supra* note 8, pts. I & IV, paras. 1–28, 573–632.

233. Panel Report, *European Communities – Measures Affecting the Approval and Marketing of Biotech Products*, WT/DS291/R, WT/DS292/R, WT/DS293/R (Sept. 29, 2006) (*adopted* Nov. 21, 2006) (with more than 800 pages).

234. *See* Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R (Mar. 3, 2005) (*adopted* Mar. 21, 2005) [hereinafter Appellate Body Report *US – Upland Cotton*] (with 295 pages). On the *Cotton* decision, see Raj Bhala & David A. Gantz, *WTO Case Review 2005*, 23 ARIZ. J. INT'L & COMP. L. 107, 214 (2006).

Annexes).[235] The Appellate Body followed that up with a ridiculously long report of 576 pages and 2,716 footnotes.[236]

As usual with Appellate Body Reports, the *Airbus* Report is not organized to be user-friendly. Rather than start logically with the salient facts on which the case turned, the Appellate Body gives a sketch introduction and then launches into a 237-page regurgitation of the arguments of the United States, the EU, and third parties. In the third part of the Report, it presents the issues. Only at page 244 does the Appellate Body deign to discuss the facts. Thus, no reader new to the case, nor any reader with a passing familiarity of it, rationally would or could read the Report in sequence. Rather (and ironically), the Report has to be read like a dictionary, choosing carefully which pages to read and in what order.

b. Who Is the Worst Offender?

The *Airbus* Appellate Body Report is the first result in a punch-counterpunch sequence between the United States and the EU. The United States complained against European subsidies to Airbus, and the EU hit back with a complaint against U.S. subsidies to Boeing. Given the length of both Appellate Body Reports, and of this Review of the Airbus report, it is worth stating up front the "bottom line." What did the Appellate Body decide and which respondent was the worst offender of GATT-WTO subsidy disciplines? The answer:

- In the June 2011 *Airbus* Report, the Appellate Body held that the EU, France, Germany, Spain, and the United Kingdom provided illegal subsidies to Airbus. These subsidies took three principal forms: 1) launch aid loans, 2) infrastructure support, and 3) equity infusions.
- The adverse trade effects caused by the illegal Airbus subsides to the United States (i.e., to Boeing) were the loss of sales of 342 aircraft worth $22 billion and the displacement of Boeing aircraft in many markets, including the EU and China, which are among the largest large civil aircraft (LCA) markets in the world.
- In the March 2012 *Boeing* Report, the Appellate Body held that the United States provided illegal subsidies to Boeing. These subsidies took five major forms:
    1) A subsidy worth $2.2 billion from the Foreign Sales Corporation scheme and Extraterritorial Income Exclusion Act;

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235. *See* Panel Report, *United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)*, WT/DS353/R (Mar. 31, 2011). This dispute will be covered in the 2012 *WTO Case Review*.

236. *See* Appellate Body Report, *United States – Measures Affecting Trade in Large Civil Aircraft (Second Complaint)*, WT/DS353/AB/R (Mar. 12, 2012) (*adopted* Mar. 23, 2012).

2) Subsidies worth $2.6 billion through procurement contracts issued by the National Aeronautics and Space Administration (NASA) and use of the facilities, equipment, and staff of NASA at no charge to Boeing;
3) Subsidies worth between $100 million and $1.2 billion via payments from the Department of Defense (DOD) and free use of DOD facilities;
4) Support from the state of Washington and city of Everett, Washington, between 1989 and 2006 totaling $16 million through the Business and Occupation tax reductions and credits; and
5) Support from the state of Kansas and city of Wichita, Kansas, totaling $476 million through the floatation of Industrial Revenue Bonds.[237]

In short, for all the heated rhetoric spouted by the United States and the EU concerning subsidies to large civil aircraft, the fact is that in using different types of subsidy schemes, both ran significantly afoul of multilateral rules on subsidies, but the EU violations were more egregious if measured in outright dollar terms. To be sure, both sides overstated their cases, as the Appellate Body determined the number of subsidy schemes and attendant trade damage was considerably less than that alleged by the respective complainants. Still, the damage inflicted on Boeing by European subsidies was on the order of five times greater than that inflicted on Airbus by American subsidies to Boeing (roughly $22 billion versus $4 billion).[238]

c. History of Airbus[239]

Airbus Industrie did not exist until 1970. In that year, it was formed as a consortium of aerospace companies from France, Germany, Spain, and the United Kingdom and operated as such until 2001. The consortium companies as of the 1970 founding included:

- From France, Aérospatiale Société Nationale Industrielle (Aérospatiale).
- From Germany, Deutsche Airbus GmbH (Deutsche Airbus).
- From Spain, Construcciones Aeronáuticas SA (CASA).

237. *See* Daniel Pruzin, *Transportation: WTO Formally Adopts Boeing Ruling; Clock Starts Ticking on Compliance*, 29 INT'L TRADE REP. (BNA) 481 (Mar. 29, 2012).

238. *See id.*

239. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 573–582.

In 1979, the British Aerospace Corporation joined the consortium.[240] Many corporate restructurings occurred between 1979 and 2000 affecting Aérospatiale, Deutsche Airbus, and British Aerospace. Nonetheless, the shareholdings (discussed below) in the consortium remained the same.

The consortium companies sometimes were referred to as "partners" in the consortium, and the terms "Airbus Industrie" and "Airbus consortium" are interchangeable. The consortium operated in a partnership arrangement through a French entity called Airbus GIE.[241] So the terms "Airbus Industrie" and "Airbus consortium" refer collectively to the partners in Airbus and the Airbus GIE entity.[242]

As summarized in the Table 1, each partner in the Airbus consortium held the following interests in the over-arching partnership, Airbus GIE.

Table 1: Shares in Airbus (1979–2000)

Country	**Partner in the Consortium**	**Percentage of Shares Held**
France	Aérospatiale	37.9%
Germany	Deutsche Airbus	37.9%
Spain	CASA	4.2%
United Kingdom	British Aerospace	20%

Note that Airbus GIE was not itself engaged in production activities. Rather, each Airbus partner produced specific parts of various models of Airbus LCA. Airbus GIE coordinated those manufacturing activities, allocated sales revenues and profits to the partners, and took responsibility for marketing, sales contracts, aircraft delivery, and customer service.

In 2000, the Airbus partners from France, Germany, and Spain merged their activities in the aeronautics, defense, and space activities. The governments took all of their shares in their respective companies (Aérospatiale, Deutsche Airbus, and CASA) and created under Dutch law a public limited liability company called the European Aeronautic Defense and Space Company NV, typically referred to as EADS. The percentage shareholding stake each government received in EADS was in proportion to the relative values of the shares of their respective companies that they put into EADS. British Aerospace continued to hold a 20% interest in Airbus GIE.

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240. In 1999, British Aerospace merged with Marconi Electronic Systems to form BAE Systems. Herein, the pre- and post-merger entity is referred to as British Aerospace. *See id.* xv (List of Abbreviations), para. 6 n.33.

241. GIE is the acronym for *groupement d'intérêt économique*. *See id.* para. 577 n.1376.

242. Occasionally the Appellate Body refers to the separate French entity Airbus GIE to distinguish it from the consortium partners from France, Germany, Spain, and the United Kingdom. *See, e.g., id.*, paras. 577–578. This distinction is not used here.

In 2001, EADS and British Aerospace put all of their assets and operations related to Airbus and their shares in Airbus GIE into a new holding company, Airbus SAS.[243] This new company was organized under French law, and the Airbus assets and operations, and shares in Airbus GIE, were under the common control of Airbus SAS. Thus, for example, the assets related to LCA located in France, Germany, Spain, and the United Kingdom were transferred to Airbus SAS, specifically to subsidiaries of Airbus SAS located in those respective countries. The LCA assets of Aérospatiale shifted to Airbus France SAS. The LCA assets of Deutsche Airbus moved to Airbus Deutschland GmbH. The LCA assets of *CASA* were transferred to Airbus España. British Aerospace transferred its LCA-related assets to Airbus SAS, in exchange for a 20% stake in Airbus SAS. Then, Airbus SAS transferred those assets to Airbus U.K.

With these transactions completed, EADS held an 80% stake in Airbus SAS, and thus wielded effective control over Airbus operations. British Aerospace held a 20% stake with specific minority rights. The last major corporate transaction occurred in 2006, when EADS bought this 20% stake from British Aerospace, making Airbus SAS a wholly owned subsidiary of EADS.

3. Synopsis of Key Facts and Conclusions

In any event, the United States took aim at over 300 separate instances of alleged subsidies to Airbus SAS (Airbus) across roughly forty years.[244] These subsidies (as discussed in Part II.C.4.a.–d. of this Case Review) were granted by the EU or in some instances by governments of four EU countries; namely, France, Germany, Spain, and the United Kingdom.

With respect to the vast array of disputed subsidies, the Appellate Body held that under Articles 5(c) and 6 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement),[245] support falling into one of four broad categories of subsidy measures was actionable (Yellow Light) because they were specific to Airbus, conferred a benefit to Airbus, and caused serious prejudice to the United States.[246] There were also several categories of prohibited

243. SAS is the French acronym for *société par actions simplifiée*. *See id.* para. 582.

244. The Panel found that "Airbus SAS" was the same as the "*Airbus Industrie*" consortium, regardless of the changes in corporate structure that had occurred through the decades. So subsidies to any entity in the consortium constituted support for Airbus LCA. This finding does not appear to have been contested on appeal. *See* WTO DS316, *supra* note 232, para. 7.286.

245. *See* Agreement on Subsidies and Countervailing Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 410 (1994) [hereinafter SCM Agreement], *available at* http://www.wto.org/english/docs_e/legal_e/legal_e.htm#wtoagreement.

246. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1230–1300 (discussing the law and evidence of causation under Articles 5 and 6 of the SCM Agreement).

(Red Light) subsidies.[247] We note that the practical legal difference between Red Light and Yellow Light subsidies is that with Yellow Light subsidies, the Claimant Member must show that the subsidies result in "adverse effects" to the Claimant,[248] while Red Light subsidies are per se illegal and require no showing of adverse effects.[249] This makes it less difficult to prevail in WTO litigation when Red Light subsidies are being challenged.

Within each general category, there were many measures. The five categories and the measures in them that the Panel and Appellate Body agreed were legally problematic:

a. Launch Aid Measures (Member State Financing)[250]

Launch Aid (also called Member State Financing) is funding for the design and development of specific models of Airbus aircraft. France, Germany, Spain, and the United Kingdom gave these subsidies to Airbus for the development of the entire fleet of large civil aircraft made by Airbus. That fleet consists of six LCA models: A300, A310, A320, A330/A340 (including the variants of the A330/A340; namely, A330-200 and A340-500/600), A350, and A380. The A380 is the massive aircraft equivalent to roughly two Boeing 747 jumbo jets and is capable of carrying roughly 600 passengers.

The United States argued that all forms of Launch Aid provided to Airbus qualified as a "subsidy" under the definition of that term in the SCM Agreement; namely, each form was a "financial contribution" under Article 1:1(a)(1)(i), which conferred a "benefit" on Airbus under Article 1:1(b). Moreover, said the United States, all Launch Aid was "specific" to Airbus under Article 2. These provisions state:

Article 1: Definition of a Subsidy

> 1.1. For the purpose of this Agreement, a *subsidy* shall be deemed to exist if:
>
> (a)(1) there is a *financial contribution* by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e., where:

247. *Id.* para. 1416.

248. SCM Agreement, *supra* note 245, art. 5.

249. *Id.* art. 4.

250. The Panel and Appellate Body abbreviated references to this kind of subsidy as "LA/MSF." *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1(a) n.6. The Appellate Body sets out a detailed discussion of Launch Aid facts. *See id.* paras. 583–610.

(i) a government practice involves a *direct transfer of funds* (e.g., grants, *loans*, and equity infusion), *potential direct transfers of funds* or liabilities (*e.g., loan guarantees*);

(ii) government revenue that is otherwise due is foregone or not collected (e.g., fiscal incentives such as tax credits);

(iii) a government provides goods or services other than general infrastructure, or purchases goods;

(iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments;

or

(a)(2) there is any form of income or price support in the sense of Article XVI of GATT 1994;

and

(b) a *benefit is thereby conferred*.

1.2. A subsidy as defined in paragraph 1 shall be subject to the provisions of Part II or shall be subject to the provisions of Part III or V only if such a subsidy is *specific* in accordance with the provisions of Article 2.

Article 2: Specificity

2.1. In order to determine whether a subsidy, as defined in paragraph 1 of Article 1, is specific to an enterprise or industry or group of enterprises or industries (referred to in this Agreement as "certain enterprises") within the jurisdiction of the granting authority, the following principles shall apply:

(a) Where the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific.

(b) Where the granting authority, or the legislation pursuant to which the granting authority operates, establishes objective criteria or conditions governing the eligibility for, and the amount of, a subsidy, specificity shall not exist, provided that the eligibility is automatic and that such criteria and conditions are strictly adhered to. The criteria or conditions must be clearly spelled out in law, regulation, or other official document, so as to be capable of verification.

(c) If, notwithstanding any appearance of non-specificity resulting from the application of the principles laid down in sub-paragraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of a subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy. In applying this sub-paragraph, account shall be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority, as well as of the length of time during which the subsidy programme has been in operation.

2.2. A subsidy which is limited to certain enterprises located within a designated geographical region within the jurisdiction of the granting authority shall be specific. It is understood that the setting or change of generally applicable tax rates by all levels of government entitled to do so shall not be deemed to be a specific subsidy for the purposes of this Agreement.

> 2.3. Any subsidy falling under the provisions of Article 3 shall be deemed to be specific.
>
> 2.4. Any determination of specificity under the provisions of this Article shall be clearly substantiated on the basis of positive evidence.[251]

What were the forms of Launch Aid at issue? There were many. Launch Aid took the form of actual and potential direct transfers of funds, under Article 1:1(a)(1)(i). That is, Launch Aid amounted to payments to Airbus on preferential terms. It also took the form of the assumption or forgiveness of some of the debt incurred by Airbus in connection with Launch Aid and LCA development and production financing.

Put succinctly, the United States said the common features of all Launch Aid were these: unsecured loans to Airbus to develop new aircraft models at below market interest rates and on repayment terms that were back-loaded and success-dependent (i.e., dependent on the success of Airbus aircraft sales).[252] Over time, the proportion of development costs funded by such loans declined, from nearly 100% for the early models (A300 and A310), to between 64% and 85% for the A300/A310, to 33% for the A33-200, A340-500/600, and A380.[253]

With respect to the interest rate, the percentage varied depending on the contractual arrangement (discussed below) for Launch Aid to one model of Airbus aircraft versus another.[254] For some models, Launch Aid was provided free of any interest. For other models, the rate varied, and different formulas were used to calculate the interest depending on the model.

Regarding disbursement, in some instances—again, depending on the contractual arrangement—Airbus received Launch Aid before incurring actual development costs on the basis of projected expenditure by Airbus.[255] In other instances, Airbus received Launch Aid after incurring costs. That is, Aid funds could be provided in one of two ways: up front, before any actual development costs were incurred, based on projected expenditure; or disbursement up to agreed amounts after actual costs were incurred.[256]

As for repayment, in most cases, Airbus was contractually obligated to reimburse all Launch Aid funds, plus interest, exclusively from revenues generated by sales and deliveries of the particular Airbus aircraft model for which it received financing.[257] In particular, Airbus was obliged to repay all funding, with interest at a contractually agreed rate, exclusively from revenues it earned by delivering a model of LCA that received financing.

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251. SCM Agreement, *supra* note 245, arts. 1–2 (emphasis added) (footnotes omitted).
252. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 604.
253. *Id.* para. 605.
254. *See id.* para. 608.
255. *See id.* para. 606.
256. *See id.* paras. 823–824.
257. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 607.

Consequently, the Panel described Launch Aid as "unsecured," as there was no guarantee Airbus could repay the Aid in full if it did not make the number of LCA sales and deliveries needed to generate the requisite funds.[258] Moreover, the Panel observed that the scheduled repayments were not collateralized by any lien on Airbus assets, nor guaranteed by a third party. And all funding was non-recourse, so the lending governments could not make claims on Airbus if Airbus failed to repay its obligations.

The payments tended to take the form of a per-aircraft levy and followed a pre-established repayment schedule, with the first payment coinciding with delivery of the first aircraft or after delivery of a specified number of deliveries. Once Airbus started repaying the Launch Aid, the amounts graduated on an ascending scale; i.e., repayments on the first aircraft deliveries were lower than repayments on later deliveries. (The exact degree of graduation in the scale varied from one Airbus model to another.) For certain, Launch Aid connected to the A340-500/600 from the Spanish government, and Launch Aid from the British, German, and Spanish governments for the A380, accelerated repayment provisions applied. Further, some Launch Aid contracts called for Airbus to pay royalties to the creditor governments if Airbus made deliveries of aircraft in excess of the number Airbus needed to secure repayment. Such royalties were defined either as a specified percentage of the price of aircraft sold on deliveries above a specified threshold or as gradually increasing sums on aircraft deliveries above a certain level.

Regardless of its form, France, Germany, Spain, and the United Kingdom provided Launch Aid through one of two types of contractual frameworks: an inter-governmental arrangement plus direct, bilateral arrangements, or through just direct, bilateral arrangements.[259] That is, under the first type, there were two sets of contracts:

- A general inter-governmental agreement among contracting parties (i.e., general agreements among France, Germany, Spain, and the United Kingdom) that specified the relative commitments of each country to fund the development of a particular model of LCA.
- Related separate contracts between the government of each country and the Airbus entity in its territory to implement Launch Aid financing at the national level.

The purpose of any inter-governmental arrangement was to specify key terms and conditions of Launch Aid, such as the amounts to be disbursed by and the modes of repayment to each government. Under the second type of

258. *See id.* para. 825.

259. For a tabular summary of the dizzying array of Launch Aid contracts, see *id.* para. 603 tbl.2. The table may contain inaccuracies. For example, the A330/340 Agreement is dated as 1995, when in fact it is from 1994. *See also id.* para. 822 (where the Appellate Body unnecessarily repeated its description from Section IV.C. of its Report concerning contractual frameworks, thus making the Report longer).

contractual framework, there was no inter-governmental agreement. Rather, there were only individual contracts between each government and the Airbus entity in its territory.

Launch Aid for several Airbus models followed the first contractual framework. For instance, in one arrangement, called the "1969 A300 Agreement," France and Germany agreed to fund the development of the A300 through loans, which Airbus would repay via graduated levies on the sale of each aircraft. Subsequent arrangements followed the 1969 template but with some deviations. For example, the "1981 A310 Agreement" embodied the core principles of the 1969 and 1971 Agreements for the A300 and applied them to the development of the A310. In the 1981 Agreement, France, Germany, Spain, and the United Kingdom provided A310 funding through loans to be repaid via graduated levies on aircraft sales. It also specified the amount of A310 development costs that Belgium and the Netherlands would bear. Significantly, with respect to the A300 and A310, the Agreements made clear that the costs of production of aircraft were not to be financed by the governments, but rather by the manufacturers themselves (e.g., British Aerospace, Deutsche Airbus, etc.).

The contractual framework for the A320 and A330/340 Airbus models was like that for, but less precise than, the A300 and A310 projects. They—including the 1991 A320 Agreement and 1994 A330/340 Agreement—set out the financial contributions expected from the governments of Belgium, France, Germany, Spain, and the United Kingdom, and stated that repayments would come from aircraft sales revenues. But these inter-governmental accords did not specify the form, value, or timing of the payments. Again, production costs were not financed under these accords but remained the responsibility of the manufacturers. Notably, the 1994 A330/340 Agreement said that the British, French, German, and Spanish governments would support export financing (with the Spanish government limiting its export support to purchases of the A330/340 by Spanish airlines).

For various other Airbus models, the second type of contractual framework was used. For example, for the A330-220 and A340-500/600 models, there were no inter-governmental agreements. That also was true for the A380, though in 2003, France, Germany, Spain, and the United Kingdom reached the "2003 Agreement" with Airbus SAS. It contained general principles and obligations for all Airbus models, especially the A380. For the A330-220, A340-500/600, and A380, governments entered into separate, national-level contracts with the manufacturers; namely, Aérospatiale, CASA, Airbus France, Airbus Deutschland GMbH, EADS Airbus, and British Aerospace. That is, these models followed the second type of contractual framework.

Neither before the Panel nor on appeal did the EU contest the American argument that Launch Aid satisfied the "financial contribution" test in Article 1:1(a)(i) or that it was "specific" under Article 2. Rather, the EU argued that none of its Launch Aid conferred a "benefit" to Airbus under Article 1:1(b).

b. Preferential Lending Measures[260]

The European Investment Bank (EIB) provided twelve loans to Airbus on off-market terms between 1998 and 2002 for the design and development of aircraft. In particular, the loans fell into the following categories: 1) a 2002 loan to EADS for research and development (R&D) activities for the Airbus A380; 2) three loans to Aérospatiale to produce Super Transporteurs aircraft in 1993, and to pay for facilities and equipment in 1988 and 1992 for the A330/A340; 3) four loans to British Aerospace to design, develop, and manufacture wing boxes for the A330 and A340 in 1990 and 1991, and to design and develop wings for the A320 in 1988 and 1989; 4) three loans to CASA, one in 1989 and two in 1990, to design and produce various parts for the A320 and A330/340; and 5) a 1990 loan to Airbus GIE for R&D of the A321.

c. Corporate Restructuring Measures[261]

France and Germany provided equity infusions and grants to companies that joined in the consortium to form Airbus. They also forgave the debt of Airbus. The French and German central governments did so through government-owned and government-controlled banks.

France provided five equity infusions to Aérospatiale in 1987, 1988, and 1994. These transactions were capital investments in Aérospatiale; namely, of French francs (FF) 1.25 billion in 1987, another FF1.25 billion in 1988, and FF2 billion in 1994. Crédit Lyonnais made one such capital contribution in 1992. Crédit Lyonnais took a 20% equity interest in Aérospatiale, which had been wholly owned by the French government until then, paying FF1.4 billion for a mixture of newly issued shares and shares from the government. For the shares held by the government, Crédit Lyonnais paid the government 2% of its own share capital (i.e., a stock-for-stock, rather than stock-for-cash, acquisition).

Further, on December 30, 1998, France transferred its 45.76% equity interest (and all associated voting rights) in Dassault Aviation to Aérospatiale (i.e., Airbus). The French government had acquired this stake in 1978 from a privately held producer of business, regional, and military jets. With this stake, due to certain double voting shares, the French government had a controlling interest in Dassault. With the transfer of the shares to Aérospatiale, those double-voting rights were cancelled.[262]

In return, Aérospatiale agreed to issue new shares of its stock at a later date, once a panel of independent experts agreed on a fixed exchange ratio. The panel gave its report on March 19, 1999, setting an exchange ratio of two Aérospatiale shares for each Dassault Aviation share. The panel agreed with the

260. *See id.* paras. 1(b), 610.

261. *See id.* paras. 1(d), 578 n.1382. The Appellate Body sets out the corporate restructuring measures in detail. *See id.* paras. 629–632.

262. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 631, 1013.

contribution of Dassault Aviation shares to Aérospatiale at an amount equal to their net book value of FF2.658 billion. And, on May 6, 1999, Aérospatiale issued 9,267,094 new shares to the French government.

This entire transaction was part of a larger French government plan to consolidate the French aeronautical, defense, and space industries by combining Aérospatiale with Matra Hautes Technologies (MHT), a French government-owned corporation. The combination occurred in 1998, and in 1999, France partially privatized the entity, Aérospatiale-MHT, resulting in it holding 48% of the shares, with employees, a private company, and the public holding the remaining 2%, 33%, and 17% stakes, respectively.

As for Germany, in the late 1980s, the central government restructured Deutsche Airbus. That restructuring involved three controversial transactions that the United States charged involved subsidization, the first two of which the Appellate Body agreed: 1) the 1989 acquisition by the German government, through its development bank, Kreditanstalt für Wiederaufbau (Credit Agency for Reconstruction, or KfW), of a 20% equity interest in Deutsche Airbus; 2) the 1992 sale by KfW of that interest to Messerschmitt-Bölkow-Blohm GmbH (MBB), which is the parent company of Deutsche Airbus; and 3) the 1998 forgiveness of 7.7 billion Deutschmarks (DM) of debt owed by Deutsche Airbus to the German government.

Also challenged by the United States was the 1998 agreement of the German government to accept a payment of DM1.75 billion from Deutsche Airbus to settle outstanding claims after the restructuring of that company. The United States argued that the total accumulated principal amount of the debt that Deutsche Airbus owed to its government was at least DM9.4 billion. Hence, said the United States, the transaction was one of debt forgiveness worth DM7.7 billion.

d. Infrastructure Measures[263]

From EU countries, Airbus received goods, services, and grants to establish, expand, and upgrade its manufacturing sites, specifically so it could develop and produce the A380.

In particular, the German central government provided assistance to Airbus to lease land near Hamburg, Germany, reclaimed from Mühlenberger Loch (Lake Mühlenberger). In 2000, the city of Hamburg decided to turn wetlands at the lake into usable land. In February 2001, Hamburg began building new dykes and upgrading the height of dykes around the Airbus facility in the area. The dyke enhancements provided flood protection for reclaimed land. Further, Hamburg built special purpose facilities on the reclaimed land; namely, a quay, sluice, and

263. *See id.* paras. 1(c), 622–628 (setting out a detailed discussion of the infrastructure measures).

pump building; a drainage ditch; a roll-on-and-roll-off area; and a sternfender. The total cost to Hamburg was €751 million.[264]

In turn, Hamburg leased the reclaimed land to Airbus Germany through a scheme known as Projektierungsgesellschaft Finkenwerder GmbH & Co. KG, or ProFi. The annual lease rate was €3.60 per square meter (adjusted based on the German Consumer Price Index). Additionally, via ProFi, Hamburg and Airbus Germany concluded four lease agreements for the special purpose facilities for twenty years. These leases called for a rental rate to assure Hamburg would get a 6.5% rate of return on its investment in each facility; namely, an annualized sum of €5,619,200 (adjusted for inflation).

Germany also supported the right of Airbus to exclusive use of an extended runway at the airport in Bremen, Germany, and assisted with noise-reduction measures relating to the lengthening of the runway. In 1989-1990, the city of Bremen extended the runway by 300 meters at either end, from 2,034 to 2,634 meters, to comply with EU requirements for a safety margin. Bremen bore the cost of both the runway extension and noise-reduction measures; namely, DM40 million and DM10 million, respectively.[265] Significantly, with the exception of emergencies, the Bremen runway is for the exclusive use of flights transporting Airbus wings from Bremen.

Also in Germany, subcentral governmental authorities in Nordenham gave regional grants to Airbus. That is, the German Land of Lower Saxony provided money for Airbus to expand its facility at Nordenham.

In France, the central government provided to Airbus the Aéroconstellation industrial site in Toulouse and improved the road relating to that cite. In particular, in 1999, government officials authorized the development of an industrial site next to the Toulouse-Blagnac Airport for the exclusive purpose of aeronautical activities. The government zoned the site a *zone d'aménagemement concertée* (ZAC), which means the government buys, improves, and sells the land for economic development.

For the ZAC Aéroconstellation industrial site, the French government had to convert agricultural land to land for industrial use; hence, it had to put in drainage, sewage, and water circulation systems, and equip the property with fencing, fire protection, landscaping, and lighting. The government also established specialized facilities, called *équipement d'intérêt general* (EIG). The EIGs were infrastructure specially designed for aeronautical activities; namely, aircraft parking areas, service areas, taxiways and roads, and underground technical galleries.

Once the French government completed the ZAC Aéroconstellation industrial site, it sold all but eleven hectares of the site to different aeronautical companies, including ones involved in the development and production of the Airbus A380. Buyers included Airbus France and Air France Industries. The buyers, all of which paid the same square meter price for differently sized plots,

264. The EU countered that the actual cost was €694 million. *Id.* para. 623.

265. The EU disputed these figures. *Id.* para. 625.

formed an association called AFUL (Association Foncière Urbaine Libre). Then, the city of Toulouse authorities leased the EIG facilities to AFUL, the members of which paid rent for the facilities based on their respective usage of them. Only AFUL members could use the EIG facilities.

Also during the late 1990s and early 2000s, the French government improved several roads around the Aéroconstellation site, particularly to link the site to an extra-wide highway (an *itinéraire à grand gabarit*, or IGG). The IGG was used by Airbus to transport A380 components produced elsewhere from the French coast to the Aéroconstellation site for use by the AFUL members.

Likewise, in Spain, the subcentral governments of Andalucia and Castilla-La Mancha each gave regional grants to Airbus. These grants allowed for the expansion and modernization of Airbus and EADS plants in Sevilla, Illescas, La Rinconada, Puerto Real, Puerto de Santa Maria, and Toledo.

In the United Kingdom, Welsh authorities gave Airbus infrastructure support—again, a grant—for its facility in Broughton.

e. Research and Technological Development Measures[266]

This subsidy involved funding in the form of grants and loans for research and technological development (R&TD) from the EU and from France and Spain at the central and subcentral governmental levels to Airbus for research. In particular, R&TD funding to Airbus took six different forms:

1. Grants under the Second, Third, Fourth, Fifth, and Sixth European Communities (EC) Framework Programs, which spanned from 1987 through 2006, and were regulated by decisions from the EU Council. Those decisions set out the type of research that would be funded (e.g., under the Second Program, pre-competitive research on airplanes and helicopters; under the Third Program, environment-related technologies, aircraft operation, aerodynamics and aerothermodynamics, aeronautical structures and manufacturing, avionic systems, and mechanical, utility, and actuation technologies; under the Fourth Program, transport means plus two other fields; under the Fifth Program, acquisition of critical technologies, technology integration for new generation aircraft, and operational efficiency and safety; and under the Sixth Program, aeronautics and space research on aircraft safety, emissions, and operational capacity and safety of the air transport system). Those decisions also stated the fund amounts for identified research areas (called "indicative allocations"). The allocated funds were denominated in European Currency Units (ECU) (such as ECU500 million in the Second

266. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1(e), 611–621 (setting out a detailed discussion of R&TD funding).

Program; ECU663 million in the Third Program; ECU1.617 billion and ECU230.5 million, allocated to specific types of research in the Fourth Program; and at least ECU700 million in the Fifth Program); or in euros (such as €1.075 billion for aeronautics and space research under the Sixth Program).[267]

2. French government funding worth €1.2 billion between 1986 and 2005 for civil aeronautics research, split (according to seven reports from the French Senate on which the United States relied in its pleadings) between €391 million from 1986 to 1993 and €809 million from 1994 to 2005;
3. German government aid worth €217 million under its Luftfahrtforschungsprogramm (Aviation Research Program, or LuFo) I, II, and III, which covered three successive periods between 1995 and 2007;
4. Spanish government loans under the Plan Tecnológico Aeronáutico (PTA) I and II Programs covering successive periods from 1993 to 1998, and over €60 million in loans starting in 2000 pursuant to the Programa de Fomento de la Investigación Técnica (PROFIT, or Funding Program for Technological Research);
5. British government grants from 1992 to 2005 under the Civil Aircraft Research and Development Program (CARAD), which later became the Aeronautics Research Program (ARP); and
6. Three grant programs run by the subcentral governments of Bavaria (starting in 1990 through at least 2000 for an array of LCA-related R&TD projects), Bremen (valued at €11 million for Airbus materials and system technologies), and Hamburg.

Before the Panel, the United States challenged every measure in these categories as a specific subsidy that satisfied the tests for "financial contribution," "benefit," and "specificity" under Articles 1 and 2 of the SCM Agreement and alleged that the measures caused adverse effects to the United States under Articles 5 and 6 of the Agreement. In other words, the United States contended that every measure was an actionable, or Yellow Light, subsidy. The Appellate Body held that all the aforementioned subsidy measures in the six categories to be actionable, or unlawful, Yellow Light support. Further, the United States argued that certain Launch Aid measures were prohibited under Article 3 of the Agreement. That is, the United States highlighted a few Launch Aid measures as Red Light subsidies.

At the same time (as discussed more fully in Part II.C.4.c. of this Case Review), the Appellate Body made clear that not all subsidies from the EU or EU countries about which the United States complained were actionable and caused serious prejudice under Articles 5(c) and 6 of the SCM Agreement. Indeed, the Appellate Body ruled that some types of support under these categories did not

267. *Id.* paras. 613–617.

even satisfy the specificity test of Articles 1 and 2 of the Agreement. And no serious prejudice existed (or was proved to have occurred by the United States) with respect to the following three types of schemes:

- Certain corporate restructuring measures; namely, the 1998 transfer of a 45.76% equity interest in Dassault Aviation by France to Aérospatiale (i.e., Airbus).
- Certain infrastructure measures; namely, the special purpose facilities at the Mühlenberger Loch industrial site in Hamburg, and the Aéroconstellation industrial site and related facilities (such as parking and taxiways) in Toulouse.
- Various R&TD measures; that is, loans and grants to support Airbus research and development of LCA, specifically:
  - Loans under the Spanish PROFIT Program;
  - Grants under the Second, Third, Fourth, Fifth, and Sixth European Communities Framework Programs;
  - Grants by France between 1986 and 1993;
  - Grants by Germany under the LuFo I, II, and III Programs;
  - Grants by Bavaria, Bremen, and Hamburg; and
  - Civil aircraft research and development and aeronautics research programs by the United Kingdom.

In excluding the above-listed schemes from the scope of its Yellow Light findings under Articles 5(c) and 6, the Appellate Body largely agreed with the conclusions of the Panel. But the Appellate Body reached its conclusions for different reasons. Of course, regardless of the rationale, the net result was a partial victory for the EU, as not all of the subsidy schemes challenged by the United States were held illegal. Moreover (as discussed more fully in Part II.4.e.2. of this Case Review), the Appellate Body reversed the Panel's finding that Launch Aid to the Airbus A380 was a Red Light subsidy.

4. Five Key Appellate Issues and Holdings

On appeal, there were five key substantive issues:[268]

268. This discussion is drawn from WTO DS316, *supra* note 232. In addition to the major substantive issues discussed above, the Appellate Body was faced with and decided the following procedural issues, all of which concerned the Terms of Reference of the Panel:

1) Temporal scope of the case; namely, whether the Panel or Appellate Body could rule on certain controversial subsidies because they were granted before the SCM Agreement entered into force on January 1, 1995, or because they were grandfathered under Article 2 of the 1992 GATT Agreement on Trade in Civil Aircraft. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 5, 571(b), 650–690, 1414(b); Agreement Concerning the Application of the GATT Agreement on Trade in Civil Aircraft of April 12,

1979 on Trade in Large Civil Aircraft, with Annexes, U.S.-E.U., July 17, 1992, T.I.A.S. [hereinafter 1992 Agreement on Large Aircraft]; *see also* Council Decision 92/496/EEC, 1992 O.J. (L 301/31) (EC), and the publication of the agreement at 1992 O.J. (L301/32). Article 2 of the 1992 Agreement on Large Aircraft states: "Government support to current large civil aircraft programmes, committed prior to the date of entry into force of this Agreement, is not subject to the provisions of this Agreement, except as otherwise provided below." The EC argued that Article 2 rendered all pre-1995 subsidies compatible with the SCM Agreement, and thus they were immunized from suit under that Agreement. The Panel rejected the EU argument, as did the Appellate Body, with some modification, stating:

> [W]e *modify* the Panel's interpretation of Article 5 of the *SCM Agreement* and consider that the "causing, through the use of any subsidy, of adverse effects" is covered by Article 5 even if it arises out of subsidies granted or brought into existence prior to 1 January 1995, and that a challenge to such subsidies is not *precluded* under the terms of the *SCM Agreement*. Accordingly, we *uphold* the Panel's conclusion . . . rejecting the European Communities' request to exclude all subsidies granted prior to 1 January 1995 from the temporal scope of the dispute.

Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 690. In other words, the alleged Red and Yellow Light subsidies granted before January 1, 1995, are within the subject matter jurisdiction of the Panel and Appellate Body. *See id.* para. 571(b); *see also id*. paras. 571(q), 1301–05 (concerning whether the Panel erred in applying Article 5(c) of the SCM Agreement by not taking into account the 1992 Agreement on Large Aircraft in its analysis of adverse effects; namely, serious prejudice and causation). Perhaps much of the discussion of this issue was unnecessary or could have been trimmed. In previous cases involving pre-privatization subsidies, the Appellate Body has examined government support provided before the entry into force of the SCM Agreement.

2) Whether (as urged by the EU) the relevant law for assessing its alleged subsidies to Airbus was the 1979 Tokyo Round Subsidies Code. The Panel rejected this argument, as did the Appellate Body. *See id.* paras. 7, 687–689.

3) Inclusion of certain alleged subsidies; namely, whether the United States properly identified in its request for the establishment of a Panel specific subsidy measures discussed by the Panel. Those measures were Research and Technological Development (R&TD) grants to Airbus by France and R&TD loans by Spain under the Programa de Fomento de la Investigación Técnica (PROFIT, or Funding Program for Technological Research). The EU said that the United States described them in its request for a Panel in overly broad, ambiguous, and excessively inclusive language. The Appellate Body agreed with the Panel that the French R&TD grants were within its reference terms, but reversed the finding of the Panel that the Spanish R&TD loans were within those terms. *See id.* para. 5 nn.30–31, 571(a), 633–649, 1414(a)–(b).

4) Inclusion of certain other alleged subsidies; namely, whether American claims about alleged unwritten launch aid and loan financing from EU countries was within the authority of the Panel and Appellate Body to adjudicate. The Appellate Body held the issue outside its jurisdiction because the United States did not identify these programs in its request for the establishment of a Panel. *See id.* paras. 5, 572(a), 1415(a)–(b).

a. Extinction or Withdrawal of Benefit[269]

In reaching its holding that several types of support in the categories of Launch Aid, equity infusions, and infrastructure measures were illegal Yellow Light subsidies and that certain subsidies were illegal Red Light subsidies, the Panel and Appellate Body had to wrestle with an argument made by the EU concerning the temporal nature of its support to Airbus.

The EU looked to the references in Articles 4:7 and 7:8 of the SCM Agreement to analyze the withdrawal of subsidies. These provisions state:

> 4.7. If the measure in question is found to be a prohibited subsidy, the panel shall recommend that the subsidizing Member withdraw the subsidy without delay. In this regard, the panel shall specify in its recommendation the time-period within which the measure must be withdrawn.
> . . . .
> 7.8. Where a panel report or an Appellate Body report is adopted in which it is determined that any subsidy has resulted in adverse effects to the interests of another Member within the meaning of Article 5, the Member granting or maintaining such subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy.

The EU contended that many of the subsidy transactions had long since concluded; therefore, the benefits of the support were "extinguished" or Airbus had "extracted" those benefits. Three corporate categories of transactions—all under the rubric of intervening events—provided the factual predicate for this EU contention:[270]

1. Cash and cash equivalents were removed from two companies that preceded Airbus (DaimlerChrysler Aerospace AG (DASA) and Construcciones Aeronáuticas SA (CASA)), thus extracting the benefits of previous subsidies.
2. Arm's length sales at fair market value of the shares of various Airbus companies occurred, such that previous subsidies did not pass through to the owners of the new entity (for instance, the 2000 sale by the French government of shares in Aérospatiale-Matra, the combination of LCA-related assets and activities of the Airbus partners to create EADS in 2000 and public offering that year of EADS shares, sales of EADS shares by, inter alia, the French

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None of these issues is discussed further herein. Likewise, claims concerning whether the Panel failed to provide a reasoned and adequate explanation for its findings under Article 11 of the DSU are not discussed. *See, e.g.*, *id.* paras. 760–762.

269. This discussion is drawn from *id.* paras. 6, 691–777.

270. *See id.* paras. 716, 718.

Government in 2001 and DaimlerChrysler in 2004 and 2006, and the exercise by BAE Systems in 2006 of its put option and sale of its 20% stake in Airbus SAS to EADS);

3. Corporate restructuring of several Airbus companies into the Airbus Industrie consortium and eventually into a single corporate entity, Airbus SAS, that produces LCA, such that previous subsidy benefits did not pass through to Airbus SAS.

Given these intervening events, the EU said the United States had the burden of proving that the subsidies passed through to these various corporate forms.[271]

To support its position, the EU cited Appellate Body pre-privatization case precedents that entailed losses by the United States and the EU, respectively: the *Bismuth Steel* and *Certain EC Products* decisions.[272] The EU said these precedents stand for the principle that a sale of a producer at arm's length and for fair market value establishes a presumption that the benefit conferred by any prior financial contributions to that producer is extinguished by that sale. The United States countered on the facts giving rise to these two precedents: they involved full privatizations and the full relinquishment of control by the governments involved. The intervening events in the *Airbus* case are partial privatizations and sales among private companies. So, said the United States, the precedents cannot be extended to the *Airbus* context.

Aside from these intervening events that extinguished the subsidies, the EU explained that the passage of time constituted a "withdraw[al]" of the subsidies. The EU urged that the extinction or withdrawal of subsidies must be taken into account when applying the SCM Agreement.[273] In particular, an adverse-effects analysis under Article 5 must change. For instance, in a serious prejudice analysis under Article 5(c), a complainant must show continuing or present benefits in the reference period under investigation (the Period of Investigation, or POI) from the now-extinguished or now-withdrawn subsidies. Or the complainant must prove some new subsidy scheme was created that provides current benefits. The EU stressed that Airbus SAS does not currently enjoy any subsidies that could cause adverse effects to the United States.[274]

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271. *See id*. para. 692.

272. *See See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 719–720; Appellate Body Report, *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom*, WT/DS138/AB/R (May 10, 2000) (*adopted* June 7, 2000) [hereinafter Appellate Body Report, *US – Bismuth Steel*] (analyzed in Raj Bhala & David A. Gantz, *WTO Case Review 2000*, 18 ARIZ. J. INT'L & COMP. L. 1, 63–74 (2001)); Appellate Body Report, *United States – Countervailing Measures Concerning Certain Products from the European Communities*, para. 139, WT/DS212/AB/R (Dec. 9, 2002) (*adopted* Jan. 8, 2003) [hereinafter Appellate Body Report, *US – Certain EC Products*] (analyzed in Raj Bhala & David A. Gantz, *WTO Case Review 2003*, 21 ARIZ. J. INT'L & COMP. L. 317, 368–92 (2004)).

273. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 691, 698–699.

274. *See id*. para. 694.

For textual support, the EU pointed out the use of the present tense in Articles 5 and 6 of the SCM Agreement, inferring that proof of a present subsidy presently causing adverse effects during the POI must be shown. In truth, the text provided no such support. The Panel rejected the EU argument, and so, too, did the Appellate Body. As the United States argued, the plain language of the text of Article 5 (and 6) says nothing about the time at which the causing of adverse trade effects must occur or about the need to prove a continuing benefit.[275]

Further, said the EU, the United States could not show that subsidies granted to Airbus SAS before 2001 had adverse effects on the American LCA industry because it could not prove continuity with respect to those subsidies.[276] Since 2001, Airbus SAS was the legal entity responsible for developing and manufacturing all Airbus LCA. Before 2001, a variety of companies formed the Airbus Industrie consortium, and under this umbrella framework, they were the responsible legal entities. The EU argued that to establish a prima facie case under Articles 5 and 6 of the SCM Agreement, the United States had to prove that benefits conferred by financial contributions to companies in the consortium before 2001 passed through to Airbus SAS after 2001. Here again, the Panel and Appellate Body rejected the EU argument.[277]

As a matter of legal strategy, the EU argument about extinction and withdrawal was a good threshold one. The EU hoped to have the adjudicators dismiss the case on the grounds that the lives of the disputed subsidies were over, and intervening events had occurred to ensure whatever specific benefits they might have conferred did not pass through to the present time. The EU appeared to have in its favor a body of Appellate Body case law on pre-privatization subsidies that stood for the proposition that showing continuity of benefits after a change in ownership was necessary to make out a case under Articles 5 and 6 of the Agreement. But the EU argument was unsuccessful. The Panel rejected this argument. So too did the Appellate Body, though not in all respects.

The Panel held that Articles 5 and 6 of the SCM Agreement do not require a complainant to prove, for purposes of analyzing adverse effects of a Yellow Light subsidy, that the subsidy "continues" or is "present" during the POI.[278] A key flaw in the EU argument was that it conflated two different concepts: the existence of a "benefit" in the context of the definition of a "subsidy" under Article 1 of the Agreement and the effects of a benefit under Article 5.[279] The former concerns the establishment of a subsidy scheme, while the latter concerns its consequences.

With this distinction in mind, the Panel ruled that a subsidy that is found to have existed need not additionally be proved to confer a present or continuing benefit on the recipient producing the subsidized product in order for that subsidy

275. *See id.* para. 700.

276. *See id.* para. 6.

277. *See id.* paras. 763–777.

278. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 571(c)(i), 693–695, 1414(d)(i).

279. *See id.* paras. 695–696.

to be potentially capable of causing adverse effects under Article 5. Those effects can occur even if the subsidy has been discontinued and is no longer present in the POI. Accordingly, the Panel held that the United States did not have to demonstrate, as part of its prima facie case, that subsidies provided to the Airbus Industrie consortium passed through to the extant producer of Airbus LCA; namely, Airbus SAS.[280] Simply put, said the Panel, it is not necessary for a proof of adverse effects under Article 5 to demonstrate the existence of a subsidy that presently confers a benefit. What happened in the past can have lingering adverse effects into the POI.

The Appellate Body agreed.[281] Whether a "benefit" exists at the time a financial contribution by a government is provided matters to determining whether that government created a "subsidy." Yet, even the language of Articles 1 and 14 (concerning, respectively, the definition and calculation of a subsidy) contemplate that benefits might be expected to flow from a financial contribution. In other words, that language is "forward-looking and focuses on future projections."[282] Thus, when adverse effects are considered, any panel "must [assess] how the subsidy has materialized over time."[283] This analysis may require consideration of the depreciation or amortization of the benefits of the subsidy that were projected ex ante and of intervening events that might have transpired after its grant.

But there is no requirement in Articles 5 or 6:3 stating that proof of a continuing benefit, in the sense of a present subsidy currently causing adverse effects, must be shown. These provisions state:

Article 5: Adverse Effects

> No Member should cause, through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1, adverse effects to the interests of other Members, *i.e.*,:
>
> (a) injury to the domestic industry of another Member;
>
> (b) nullification or impairment of benefits accruing directly or indirectly to other Members under GATT 1994 in particular the benefits of concessions bound under Article II of GATT 1994;
>
> (c) serious prejudice to the interests of another Member.

280. *See id.* paras. 571(c)(v), 693, 1414 (d)(vi).
281. *See id.* paras. 704–707.
282. *Id.* para. 707.
283. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 710.

> This Article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the Agreement on Agriculture.
>
> ***Article 6: Serious Prejudice***
>
> . . . .
> 6.3. Serious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or several of the following apply:
>
> (a) the effect of the subsidy is to displace or impede the imports of a like product of another Member into the market of the subsidizing Member;
>
> (b) the effect of the subsidy is to displace or impede the exports of a like product of another Member from a third country market;
>
> (c) the effect of the subsidy is a significant price undercutting by the subsidized product as compared with the price of a like product of another Member in the same market or significant price suppression, price depression or lost sales in the same market;
>
> (d) the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.[284]

Under these provisions, a past subsidy that has been extinguished or withdrawn may continue to cause adverse effects. Citing its precedent in the infamous *Cotton* dispute, the Appellate Body said:

> 712. The text of Articles 5 and 6 of the *SCM Agreement*, and in particular the use of the present tense in these provisions, does not support the proposition that there must be "present benefit" during the reference period. In its argumentation, the European

284. *See* SCM Agreement, *supra* note 245, arts. 5, 6 (footnotes omitted).

> Union conflates present adverse *effects*, which must be demonstrated under Article 6:3, with present *subsidization*, which need not. It is not disputed that Article 6:3 is concerned with present adverse effects. However, the requirement that the effects of subsidies be felt in the reference period, does not mean that the subsidies, and in particular the benefit conferred, must also be present during that period. In focusing on the causing of adverse effects through the use of any subsidy, Article 5 envisages that the use of the subsidy and the adverse effects may not be contemporaneous. This is supported by the Appellate Body's finding in *U.S. – Upland Cotton*, that *the provision of subsidies and their effects need not coincide temporally and that there may be a time lag*. . . .
>
> 713. For these reasons, we agree with the Panel that the United States was not required, under Article 5 of the *SCM Agreement*, to establish "that all or part of the "benefit" found to have been conferred by the provision of a financial contribution continues to exist, or presently exists" during the reference period. We wish to emphasize, however, that effects of a subsidy will ordinarily dissipate over time and will end at some point after the subsidy has expired. Indeed, as with a subsidy that has a finite life and materializes over time, so too do the effects of a subsidy accrue and diminish over time.[285]

In brief, a subsidy granted in the past materializes over time, meaning its benefits flow through time, but the life of the subsidy and benefits therefrom are finite. That flow of benefits, which ordinarily will decline and eventually end as time passes, is relevant to the analysis of adverse effects under Articles 5 and 6. But, for purposes of this analysis, there is no requirement that a complainant show the existence of a continuing benefit; i.e., there is no requirement that a complainant prove the existence of continuing benefits from a past subsidy contemporaneous with adverse effects during the POI from a past subsidy. Of

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285. Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 712–713 (citing Appellate Body Report, *US – Upland Cotton*, *supra* note 234, paras. 476, 482, 484) (emphasis added).

The Appellate Body said it modified the interpretation of the Panel as follows: the Panel took the view that the concept of a "continuing benefit" may be relevant to ascertain how the effect of a subsidy should be analyzed over time, and the Panel said such an analysis was part of the causation inquiry under Articles 5 and 6 and an assessment of the effects under these provisions. The Appellate Body said that the trajectory of the life of a subsidy is relevant to determining whether that subsidy causes adverse effects to another Member under Article 5 and that consideration should be given to the likelihood that those effects will dissipate over time and terminate. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 714–715. This hardly seemed to be much of a modification.

course, the Appellate Body devoted far too many paragraphs and pages to come to this obvious conclusion. It could have made it with a summary analysis of the text, and a simple and widely appreciated analogy about the time lag between an event and its consequences: the adverse effects of smoking include cancer, even years after a smoker has quit.

Also, with this distinction between the establishment of a "subsidy" under Article 1 and the "adverse effects" of its benefits under Articles 5 and 6 of the SCM Agreement in mind, the Panel dismissed as unfounded the EU argument that its subsidies had been extinguished or withdrawn because of a series of transactions at arm's length and fair market value.[286] Hence, the EU point that Airbus SAS enjoys no subsidies that cause adverse trade effects was wrong. For the most part, the Appellate Body agreed.

The Appellate Body thought the EU drew too strong an inference from the appellate body reports in the *Bismuth Steel* and *Certain EC Products* cases.[287] Whether a benefit from a pre-privatization subsidy expires following an arm's length privatization at fair market value depends on the facts of the case. There is a rebuttable presumption that it ceases to exist—but the presumption is rebuttable. Moreover, the Appellate Body put credence in the American point that the precedents were inapposite because they involved full privatizations with complete transfer of ownership and control. Notably, the three members of the Appellate Body (David Unterhalter, Presiding Member; Lilia R. Bautista, Member; and Peter Van den Bossche, Member[288]) openly diverged on whether a subsidy is extinguished in the context of a partial privatization or private party-to-private party sale, and each set out separate opinions within the main body of the *Airbus* Report: one said the precedents do not apply to this context, one said they might apply, and one said they probably do apply.[289] Their separate statements are one of the better crafted parts of the Report because each wrote in his or her own words and without the obfuscation of poor editing or writing by committee.

To be sure, the American victory was not complete on the topic of the life of a subsidy, intervening events, and the ramifications for the burden of proof. The Panel ruled that subsidies associated with several sales transactions involving particular Airbus companies were not extinguished and that the benefits of those subsidies had not been fully extracted.[290] The Appellate Body reversed this finding. The Appellate Body faulted the investigation by the Panel for failing to consider whether the partial privatizations from governments to private parties and sales transactions from one private party to another were conducted on arm's length terms at fair market value.[291] Likewise, it faulted the Panel for failing to

286. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 697.

287. *See id.* paras. 697–722 (particularly para. 708 n.1643) (citing Appellate Body Report, *US – Bismuth Steel*, *supra* note 272, Appellate Body Report, *US – Certain EC Products*, *supra* note 272).

288. *See id.* at p. 613 (subscription page).

289. *See id.* para. 726.

290. *See id.* paras. 571(c)(ii), 1414(d)(ii).

291. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 729–736.

consider the extent to which these transactions led to a complete transfer of ownership and control to new owners. The Appellate Body itself did not reach a definitive conclusion on extinction of benefits of these past subsidies, saying there was an insufficient factual basis for a decision.

The Panel considered whether extractions of cash from DASA and CASA removed a portion of past subsidies and said they did do so. In a ridiculously dilated discussion spanning nine pages and twenty-two paragraphs, the Appellate Body upheld this finding but opined that all or part of a subsidy could be extracted by the removal of cash or cash equivalents from the recipient of that subsidy.[292] Whether such extraction occurs requires a fact-intensive, case-by-case inquiry. One test, which the EU itself proposed but failed to satisfy, is that of the balance sheet; because a subsidy is reflected on the balance sheet of the recipient and because cash is fungible, if the cash is removed, that removal establishes a causal link between prior subsidization and cash extraction.[293]

Indeed, overall, the Appellate Body agreed with the Panel that, contrary to the assertion of the EU, cash extractions from DASA and CASA did not cause the subsidies to be withdrawn within the meaning of Articles 4:7 and 7:8 of the SCM Agreement. After all, those provisions discuss "withdrawal" of a subsidy after a final adjudication by a panel or the Appellate Body that a subsidy is prohibited (Red Light) or one that is actionable (Yellow Light) and causes adverse effects, pursuant to a recommendation by the Panel or Appellate Body. The Appellate Body added that it lacked a factual basis to decide whether the controversial sales transactions led to a withdrawal of those subsidies under the Agreement.

Finally, what about the EU argument that the United States should have to prove that the benefits of subsidies before 2001 to the Airbus Industrie consortium passed through to the current producer of LCA, Airbus SAS, after the Airbus partners restructured their relationships in 2001? The EU premised this argument on its earlier one; namely, that a subsidy is capable of causing an adverse effect during the POI only if a continuing benefit from the subsidy is proved during the POI.[294] As the EU lost that argument because of the logic of a time lag between: 1) provision of a subsidy and receipt of its benefits, and 2) the manifestation of adverse effects from the subsidy and benefits, the EU was sure to lose the argument about pass through, too.

So it did. The Appellate Body upheld the ruling of the Panel, and both cited to the 2005 *Cotton* case, in which the Appellate Body held that a pass-through analysis is not critical to assess whether significant price suppression occurs under Article 6:3(c); rather, what matters is identifying the subsidized

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292. *See id.* paras. 571(c)(iii)–(iv), 737–759, 1414(d)(iii)–(v).

293. *See id.* para. 746. A second test set up by the EU (but on which the Appellate Body did not rule, as the EU flunked the balance sheet test) is whether extracted cash has left the recipient or its shareholders permanently. A dividend payment would not remove cash from the corporation-shareholder unit, suggesting the subsidy had not been extracted by virtue of that payment. *See id.* paras. 744, 747–748.

294. *See id.* para. 771.

product and showing a causal link between the subsidy to that product, on the one hand, and adverse effects such as price suppression, on the other. The Appellate Body also cited its *Softwood Lumber* decision,[295] in which it articulated, in the context of Article 10 of the SCM Agreement and Article VI:3 of GATT, the circumstances in which a pass-through analysis is needed: "[W]here a subsidy is received by the producer of an input product and the imported product subject to the countervailing duty investigation is a different, downstream product manufactured by an unrelated producer operating at arm's length from the recipient of the subsidy."[296] In the Airbus case, the product was the same all along, LCA, and the relationship between the predecessor and current companies, Airbus Industrie and Airbus SAS, was not an arm's length one.[297] That is, Articles 5 and 6 of the SCM Agreement do not require such proof to make a prima facie case of adverse effects.[298] To generalize, no pass-through-of-benefits analysis is necessary under these provisions. A complainant need not show that previous subsidies to a predecessor of a producer currently benefit the new incarnation of the producer or have a causal connection to adverse effects.

b. Conferral of Benefit and Market Interest Rate Benchmark[299]

A subsidy is not actionable under Articles 5 and 6 of the SCM Agreement unless it meets the obvious prerequisites of being: 1) a financial contribution from a governmental body, such as the EU or an EU country; 2) confers a benefit to the recipient, such as Airbus; and 3) is specific to the recipient, again, such as Airbus. These prerequisites are found in Articles 1 and 2 of the Agreement. In the case, the Panel agreed with the American arguments on each point.[300]

First, each Launch Aid measure was a "financial contribution by a government or any public body" under Article 1:1(a)(1) of the SCM Agreement. These measures took the form of a direct transfer of funds within the meaning of that provision.

Second, the Launch Aid measures conferred a "benefit" to Airbus under Article 1:1(b) of the Agreement because each measure was provided by the EU or

295. *See* WTO Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R (Jan. 19, 2004) (*adopted* Feb. 17, 2004). On this case, see Raj Bhala & David A. Gantz, *WTO Case Review 2004*, 22 ARIZ. J. INT'L & COMP. L. 99, 178 (2005).

296. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 773.

297. *See id.* paras. 776–777.

298. *See id.* paras. 766, 777.

299. This discussion is drawn from *id.* paras. 2, 8 & pts. III, VI, X.

300. *See id.* para. 8, 829–831. Three loans for the A380 were not fully disbursed, so the Panel held that the undisbursed amounts were not "potential direct transfers of funds," but rather "loans." *See id.* para. 830.

an EU country on interest rate terms that were more advantageous than Airbus would have received from a market lender.

Third, the Launch Aid measures were "specific" under Article 2:1(a). Only on two narrow matters did the Panel reject the American arguments. First, with respect to the Airbus A350, the Panel said there was no clear, identifiable commitment to provide this model of aircraft with Launch Aid. Second (as discussed in Part II.C.4.d.2. of this Case Review), the Panel said an unwritten Launch Aid Program, beyond the formal, documented one, did not appear to exist.

On appeal, the Appellate Body had to consider whether the Panel was correct in holding that Launch Aid from the EU and loan financing from EU countries conferred a "benefit" to Airbus (for the A340 and A380 models) and the twelve loans from EIB to Airbus, based on a comparison with the rate of return a market lender would have demanded to provide Airbus with this funding.[301]

Of course, this question begs another: was the Launch Aid a "loan"? The Appellate Body accepted the characterization of the Panel, which in turn was based on that of the United States, that all Launch Aid financing was a "loan."[302] It was long-term, unsecured, and non-recourse. The lending EU governments anticipated payment out of project revenue. The details of the financing distinguished it from conventional loans. It was technically a hybrid form of funding with some equity-like features (namely, the extent to which risk was transferred from Airbus to the governments, making the latter akin to shareholders). Hence, the Appellate Body and Panel called it an "amortizing loan[]," and neither the EU nor United States quibbled about the point on appeal.[303]

Manifestly, measuring whether government support confers a benefit to a specific recipient requires a benchmark to determine whether that support is fair or unfair: it is unfair and confers a benefit if it is on terms more favorable than the benchmark. The opposite is true if it is on terms equal, or even worse, than the benchmark. In brief, much depends on the benchmark. Boasting a modern capitalist economy, it is natural for the United States to promote market benchmarks, as it did in the *Airbus* case. For instance, with respect to the twelve EIB loans, the United States said they were a direct or potential transfer of funds and thus financial contributions under Article 1:1(a)(1)(i) of the SCM Agreement.[304] They conferred a benefit under Article 1:1(b) because their terms were more favorable than the terms under comparable financing from market

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301. The Appellate Body, like the Panel before it, rejected the EU argument that in applying the concept of "benefit" under Article 1:1(b) of the SCM Agreement to Launch Aid, Article 4 of the 1992 Agreement on Large Aircraft, *supra* note 268, must be considered. The Appellate Body invoked Article 31:3(c) of the Vienna Convention on the Law of Treaties to reach this result. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 571(d)(i)–(ii), 839–855, 1414(e)(i)–(ii); Vienna Convention on the Law of Treaties, May 23, 1969, 1155 U.N.T.S. 331.

302. Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 826–827.

303. *Id.* para. 827.

304. *See id.* para. 3.

lenders. And, of course, the United States said they were specific under Articles 2:1(a) and (c) of the Agreement.

The Appellate Body again said "no," though of course it agreed with the idea that "benefit" requires a comparison, typically to the marketplace, and quoted the following passage from its 1999 *Canada – Aircraft* decision:

> We also believe that the word "benefit", as used in Article 1.1(b), implies some kind of comparison. This must be so, for there can be no "benefit" to the recipient unless the "financial contribution" makes the recipient "better off" than it would otherwise have been, absent that contribution. In our view, the marketplace provides an appropriate basis for comparison in determining whether a "benefit" has been "conferred", because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favourable than those available to the recipient in the market.[305]

Given that Launch Aid was an unsecured loan, the Appellate Body turned to Article 14(b) of the SCM Agreement to provide the most relevant method to gauge the benefit from such lending:

> ***Article 14: Calculation of the Amount of a Subsidy in Terms of the Benefit to the Recipient***
>
> For the purpose of Part V, any method used by the investigating authority to calculate the benefit to the recipient conferred pursuant to paragraph 1 of Article 1 shall be provided for in the national legislation or implementing regulations of the Member concerned and its application to each particular case shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines:
>
> . . . .
>
> (b) a loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts . . . .

305. *Id.* para. 832 (quoting Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R (Aug. 2, 1999) (*adopted* Aug. 20, 1999)).

However, the Appellate Body disagreed with the findings of the Panel concerning the rate of return a market lender would have required in exchange for launch aid and loan financing akin to the funding Airbus received from the EU and EU countries. The Appellate Body explained logically:

> A panel relying on Article 14(b) would thus examine whether there is a difference between the amount that the recipient pays on the government loan and the amount the recipient would pay on a comparable commercial loan, which the recipient could have actually obtained on the market. There is a benefit—and therefore a subsidy—where the amount that the recipient pays on the government loan is less than what the recipient would have paid on a comparable commercial loan that the recipient could have obtained on the market. There is no benefit—and therefore no subsidy—if what the recipient pays on the government loan is equal to or higher than what it would have paid on a comparable commercial loan. The amount the recipient would have paid on a commercial loan is a function of the size of the loan, the interest rate, the duration, and other relevant terms of the transaction.[306]

The Appellate Body explained that Article 14(b) suggests that timing matters.[307] The comparison between the amount a borrower pays on a government loan and the amount that borrower would pay on a comparable commercial loan the borrower actually could get in the market must be done as if the two loans were made at the same time. After all, "comparable" in that provision invites an inquiry into the market-based terms the borrower would have been charged at the time it got the government loan. In turn, because this comparison is at "the moment in time when the lender and borrower commit to the transaction," what matters is not how the loan actually performs over time, but rather how the loan is structured and risk is priced:[308]

> Such *ex ante* analysis of financial transactions is commonly used and appropriate financial models have been developed for these purposes. The analysis from a financial perspective proceeds as follows. The investor commits resources to an investment in the expectation of a future stream of earnings that will provide a positive return on the investment made. In deciding whether to commit resources to a particular investment, the investor will consider alternative investment opportunities. The investor will make its decision to invest on

306. *Id.* para. 834.
307. Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 835.
308. *Id.* para. 836.

> the basis of information available at the time the decision is made about market conditions and projections about how those economic conditions are likely to develop (future demand and price for the product, future costs, etc.). The information available will be, in most cases, imperfect. The investor does not have perfect foresight and thus there is always some likelihood, in some instances a sizeable one, that the investor's projections will deviate significantly from what actually transpires. Hence, determining whether the investment was commercially rational is to be ascertained based on the information that was available to the investor at the time the decision to invest was made. The commercial rationality of an investment cannot be ascertained on the basis of how the investment in fact performed because such an analysis has nothing useful to say about the basis upon which the investment was made. The investment could have earned a rate of return that exceeded, or was less than, the going market rate, but it was not predetermined to do so.[309]

The EU and United States agreed this approach was correct. The problem with the work of the Panel concerned the rates of return a market lender would have required to provide financing to Airbus. Accordingly, the Appellate Body held that the Panel failed to make an objective assessment of the issue, as required by Article 11 of the Dispute Settlement Understanding.[310]

But this disagreement did not represent a victory for the EU. The Appellate Body examined the calculations of the EU concerning the benefit from these subsidies and held that, even using the figures of the EU, Airbus did get a benefit. To explain, in considering the "benefit" conferred to Airbus for Launch Aid, the Panel used a project-specific risk premium, which the United States had proposed.[311] The proposal came from the American expert, one Dr. David M. Ellis, who said the risk premium was based on the sum of three components:[312]

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309. *Id.*

310. For the details of why the Appellate Body agreed that the EU allegations about the way in which the Panel measured "benefit" were properly characterized as errors under Article 11 of the DSU concerning whether the Panel made an objective assessment of the facts, as distinct from errors of application under Article 1:1(b) of the SCM Agreement, see *id.* paras. 871–881. The issue is one of the proper WTO text and provision to cite for the claim.

311. *See id.* paras. 3, 571(d)(ii), 1414(e)(ii). The Appellate Body delves into excruciating detail about the alternative market benchmarks; i.e., the risk premium proxies developed by the United States and the EU. *Id.* paras. 860–870. A summary (as provided above) would have sufficed and saved seven pages in the Report.

312. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 860–861.

1. The government borrowing rate for each EU country that provided Launch Aid; i.e., the interest rate on sovereign debt for those countries; plus
2. The general corporate risk of Airbus; i.e., the risk of default by Airbus on its Launch Aid repayment obligations; plus
3. The project-specific risk associated with a particular LCA model; i.e., the risk that there will be insufficient sales revenues generated from that model to cover the full investment and interest of the Launch Aid for that model.

The EU expert, one Professor Robert Whitelaw, agreed with the first two components, but not the way in which Dr. Ellis computed the third component.[313] The professor argued for a different project-specific risk premium that was calculated based on anticipated returns of risk-sharing suppliers that contributed to the development of an LCA model on terms similar to those agreed by the EU countries. Whereas the Ellis calculation was clear and resulted in a constant project-specific risk premium of 7% for all LCA models at issue in the case, the Whitelaw calculation was convoluted and not transparent, though it also produced a single, and lower, figure.[314]

The Panel did not like either the American or EU risk premium measures. Assuming the role of Wall Street analyst, the Panel said a variable risk premium would take into account the particularities of different LCA models better than a constant interest rate. Moreover, the Panel said the American computation overstated the level of risk, while the EU methodology understated it. And, putting itself in the chair of financial experts, the Panel offered various technical critiques, such as expressing concern that the American's 700 basis point figure improperly included management fees.[315]

So the Panel came up with its own risk premium to measure "benefit"; that is, as a market benchmark for the rate of return that market lenders would have received from providing Launch Aid, had they done so. It identified three groupings, each with a project-specific risk premium band:[316]

- Minimum project risk associated with the A300 and A310 Airbus models, essentially, less than 7%.
- Exterior upper boundary of the range of product risk for the A320, A330/A340, A330-200, and A340-500/600, with the range being greater than the premium proposed by the EU, but less than 7%.
- Internal upper boundary of the range of product risk for the A380 Airbus model, with the range being greater than the premium proposed by the EU, but less than or equal to 7%.

313. *See id.* para. 862.
314. *See id.* paras. 863–864.
315. *See id.* para. 885.
316. *See id.* para. 882.

In turn, the Panel compared its own market benchmark against the actual rates of return the EU countries obtained from their Launch Aid. The difference, of course, between the constructed market benchmark and actual returns was the "benefit" to Airbus. Essentially, the marketplace would have demanded a higher investment return for Launch Aid financing than did the governments, and therein was the "benefit" from the subsidy.

Not to have its financial acumen outshined by that of the Panel, the Appellate Body played Wall Street analyst. The Appellate Body examined the work of the Panel on evaluating the American versus EU risk premium and found several aspects of that work internally inconsistent. For instance, with respect to the first grouping, the Appellate Body did not like the fact the Panel relied on the project risk premium of 7% proposed by the United States as a boundary for each of the three groupings, even though the Panel criticized that figure as overestimating the risk of LCA projects that received Launch Aid.[317]

The Appellate Body also reviewed a 2001 scholarly finance article published in the *Journal of Economic Perspectives* that had been quoted in the Whitelaw Rebuttal Report and studied by the Panel.[318] The Panel thought that

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317. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 884, 886. For the financial critique by the Appellate Body of the second and third groupings and boundaries, see paras. 890–893. The Appellate Body summarized its critique on all three as follows:

> In sum, the Panel's reasoning in relation to the United States' proposed project-specific risk premium is internally inconsistent. The Panel dismissed venture capital financing as a source from which to derive the project risk of the projects financed with LA/MSF because it considered venture capital financing to be "inherently more risky than LA/MSF". At the same time, the Panel used the project-specific risk premium proposed by the United States—which had been derived by Dr. Ellis from the returns of venture capital financing—as a boundary for the ranges of project-specific risk premia that it established for the three groupings of LCA projects. The Panel's error is compounded in the case of the A300 and A310 because it left the upper limit of the range of the project-specific risk premium unbounded, thus potentially going beyond the level of the risk premium associated with venture capital financing. In the case of the second grouping, the Panel determined the same upper boundary for a diverse set of LCA projects, some of which were new aircraft, while others were derivatives. It also included projects launched in a time span of 13 years, during which Airbus had different levels of experience. And for the A380, the Panel used the United States' proposed project-specific risk premium as an inner boundary despite recognizing that, by the time the A380 was launched, Airbus was a very different company from the typical firm that receives venture capital. There are thus clear inconsistencies in the Panel's reasoning. This type of internally inconsistent reasoning cannot be reconciled with the Panel's duty to make an objective assessment of the facts under Article 11 of the DSU.

Id. para. 894.

318. *See id.* paras. 866, 885–888 (discussing P. Gompers & J. Lerner, *The Venture Capital Revolution*, 15 J. ECON. PERSP. 145 (2001)).

when Airbus launched its first LCA project, the A300, and its derivative project, the A310, Airbus was akin to a small, young company plagued by high levels of uncertainty; hence, Launch Aid was more like venture capital financing than debt incurred by a mature business with a track record. The Appellate Body found a contradiction in the reliance by the Panel on: 1) the 7% project-specific risk figure provided by the United States, and 2) its insistence that venture capital financing is more risky than Launch Aid.[319]

Why? Because the United States derived that figure from venture capital financing data. In other words, the Panel could not both use the American figure based on venture capital financing and then claim such financing is riskier than Launch Aid. If those were the relative risks, then the Panel ought to have picked a figure lower than 7%. The Appellate Body continued on by noting its displeasure at the asymmetry of the boundaries established by the Panel for the A300 and A310 projects: 7% was a minimum project-specific risk premium, but the Panel set no upper (maximum) boundary, meaning that the risk for those Launch Aid projects could be higher than even venture capital financing.[320] Therein lay another incongruity with the view of the Panel that venture capital was a riskier endeavor than Launch Aid.

So the Appellate Body did reverse the holding of the Panel with respect to using the American proposed project-specific risk premium.[321] That was an error under Article 11 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU); namely, a failure to make an objective assessment of facts. However, this reversal did not translate into a victory for the EU. The Appellate Body considered and rejected the EU appeal against the finding of the Panel; namely, the Panel ruling that the project-specific risk premium proposed by the EU for the A380 Launch Aid was unreliable and understated the risk premium market participants would have charged for this model of aircraft. Of course, in deciding to uphold the Panel, the Appellate Body consumed paragraphs 896 through 920, totaling roughly eleven pages, to state its own financial analysis of the EU position and its expert, Professor Whitelaw.[322]

But the bottom-line conclusion of the Panel was correct: a benefit was conferred by Launch Aid within the meaning of Article 1:1(b) of the SCM Agreement.[323] The project-specific risk premium proposed by the EU (actually, Professor Whitelaw) for use in constructing a market benchmark against which to value any benefit from Launch Aid subsidies understated the risk premium that a private market operator (i.e., a commercial bank) would have demanded Airbus pay to obtain financing on the same or similar terms that it got from the EU governments.[324] That was true for all models of aircraft receiving Launch Aid. Moreover, the Appellate Body (again agreeing with the Panel) found that the rate

319. *See id.* para. 888.
320. *See id.* para. 889.
321. *See id.* para. 895.
322. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, 896–920.
323. *See id.* paras. 929.
324. *See id.* paras. 3, 571(d)(ii)–(iii), 921–922, 924, 927, 1414(e)(ii)–(iv).

of return expected by EU countries for Launch Aid was lower not only than the rate calculated by Professor Whitelaw, but also lower (in all but two instances) than the rate of return that a market lender would have demanded even if the project-specific risk had been zero.[325] That is, the Appellate Body reasoned further that there was uncontested evidence that the rates of return obtained by the EU countries on all but two of the controversial Launch Aid measures were below a market benchmark that excluded use of a project-specific risk premium, and that the rate of return obtained by the EU countries on the other two Launch Aid measures were below a market benchmark that relied on the European project-specific risk premium. Here, then, was the conferral of a benefit:

> [A]lthough we have found several flaws in the Panel's analysis of Professor Whitelaw's project-specific risk premium, we have upheld the Panel's conclusion that this risk premium underestimates the level of risk. Thus, the appropriate level of risk premium for these projects is somewhere above the level calculated by Professor Whitelaw. *Since the appropriate project-specific risk premia – and consequently the rate of return that would have been demanded by a market lender – are higher than the level calculated by Professor Whitelaw and submitted by the European Communities, it necessarily follows that the LA/MSF [Launch Aid] measures were provided at a rate of return that was below the market benchmark and, consequently, conferred a benefit*.[326]

Simply put, the wrangling over use of the American or European risk premium proxy might be of interest to quantitatively oriented business school professors, but not most real-world lawyers. Regardless of the premium used, under any reasonable proxy for market rates, the fact remained that the European governments gave Airbus better-than-market terms on Launch Aid financing.

Concomitantly, the Appellate Body found that the Panel erred in concluding that "the number of sales over which full repayment is expected says little, if anything, about the appropriateness of the rate of return that will be achieved by the lender."[327] Actually, this proposition runs against even an intuitive understanding of finance. In assessing the payback for any type of financing, not only is it relevant to consider time, but also sales. For example, a $1 billion loan fully repaid after just one aircraft sale could be regarded as a spectacular return for the lender, while full repayment only after the sale of 100 aircraft may be viewed as inappropriately poor. As the Appellate Body rightly explained:

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325. *See id.* para. 926 n.2093.
326. *Id.* para. 927 (emphasis added).
327. Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 571(d)(iv), 1414(e)(v).

> 935. . . . [T]he assessment of benefit under Article 1.1(b) of the *SCM Agreement* calls for a comparison of the terms and conditions of the LA/MSF measures with the terms and conditions that would have been offered on the market at that time the challenged LA/MSF measures were granted. Where, as in the case of the LA/MSF measures, the re-payment of a loan depends on the number of sales, the *expected* number of sales will be a fundamental element in the computation of the rate of return of the loan. This is because the rate of return is a function of the number of sales that are forecast. Although the Panel's reasoning is not altogether clear, we understand the Panel to have taken an *ex ante* approach to the calculation of the rates of return of the member State governments, that is, the Panel calculated the rates of return expected at the time the LA/MSF measures were provided. The European Union and the United States confirmed at the oral hearing that they too understand the Panel as having taken an *ex ante* approach.
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> 936. The Panel did not explain why it considered that "the number of sales over which full repayment is expected says little, if anything, about the appropriateness of the rate of return that will be achieved by the lender." It may be that what the Panel meant is that the number of sales over which repayment is expected is not dispositive of the question of whether the rate of return demonstrates that the loan confers a benefit. Understood in this way, the statement would be correct given that the assessment of benefit would require a comparison with the rate of return that would have been demanded by a market lender. The Panel's statement, however, can also be understood to suggest that the number of sales is irrelevant to the calculation of the rate of return of the member State governments. . . . [T]his would be incorrect. Given the potential that the Panel's statement could be misused in the future, we *reverse* this statement.[328]

In sum, the Appellate Body did well to overturn what otherwise would have remained in WTO jurisprudence as one of the less intelligent financial observations by a Panel.

328. *Id.* paras. 935–936.

c. Specificity of and Benefit from Subsidies (SCM Agreement Articles 1 and 2)[329]

No subsidy is actionable (Yellow Light) or prohibited (Red Light) unless it is, indeed, a "subsidy," which means, inter alia, that it must be specific to a certain enterprise or industry. If it is generally available, then it flunks the specificity test of Articles 1 and 2:1(a) and (c) of the SCM Agreement. Were all of the subsidies to Airbus identified by the United States "specific" to Airbus, and thus covered by the SCM Agreement and potentially within the Yellow Light category? If so, then did they all contribute a "benefit" to Airbus?

Obviously, before the Panel, the United States claimed they were. That is, the United States alleged the Launch Aid was a highly preferential financing that amounted to a specific subsidy. Likewise, said the United States, the twelve loans provided by EIB to Airbus were specific. So, too, urged the United States, were the infrastructure measures of France, Germany, Spain, and the United Kingdom; the corporate restructuring (especially the German government restructuring of Deutsche Airbus in the late 1980s and the five French equity infusions to Aérospatiale); and the R&TD funding.

The debate about specificity carried on to the appellate stage. The Appellate Body had to resolve whether various types of support were generally available to any enterprise or industry, or specific to Airbus. The Appellate Body responded, as had the Panel, that many of the alleged subsidies were "specific" and conferred a "benefit," but some were not.

In particular, the Panel held that fifteen individual measures of support for Airbus, grouped under three general categories, satisfied the specificity test and conferred a benefit on Airbus.[330]

Under the general category of "Infrastructure Measures," the Panel included:[331]

- Assistance to Airbus to lease land at the Mühlenberger Loch industrial site in Hamburg.[332] The Panel said no commercial investor would have undertaken the projects there, specifically, converting wetlands to useable land, building flood protection measures, and constructing special purpose facilities. These projects were undertaken by the city of Hamburg for Airbus. A market-based purchase or reclamation of the site for investment purposes would have cost €750 million, and the investor would have sought a return on its investment. Yet, the rent Airbus paid for the site provided for no market rate of return to the Hamburg authorities. Hence, Airbus received a benefit from the industrial site.

329. This discussion is drawn from *id.* paras. 2–4, 11.
330. The findings of the Panel on specificity are summarized at *id.* paras. 937–940.
331. *See id.* paras. 11, 571(f), 1414(f).
332. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 954–956.

- Lengthening of the runway at Bremen Airport.[333] The Panel observed that the runway extension and noise reduction measures provided by the city of Bremen were done specifically to meet the needs of Airbus. Bremen did so without earning any return on its investment in the runway lengthening or noise-cutting measures, thus conferring a benefit on Airbus.
- The ZAC Aéroconstellation industrial site in Toulouse and associated EIG facilities.[334] Here again, the Panel found that the EU provided support specifically to help Airbus; namely, with respect to the site and EIG facilities, to enable it to locate an A380 final assembly line in Toulouse. The site itself, near the Toulouse-Blagnac airport and with particularized EIG facilities, was uniquely configured to meet the needs of Airbus. The benefit to Airbus took the form of the below-market price Airbus paid for the site. That price did not permit an adequate return to cover the investment of the EU in developing the site, and no commercial land developer would have undertaken the project on such terms.

These three measures, said the Panel, were a "financial contribution" under Article 1:1(a)(1)(iii) of the SCM Agreement, conferred a benefit under Article 1:1(b), and were specific under Article 2:2 because they were the provision of goods other than general infrastructure. Similarly, two further infrastructure measures were "specific" under Article 2:2:

- Grants given by the German subcentral government in Nordenham, Germany.
- Grants from the Spanish subcentral governments in Illescas, Puerto Real, Puerto de Santa Maria, La Riconanda, and Sevilla to construct manufacturing and assembly lines at several locations in those countries.

Under the general category "Corporate Restructuring Measures,"[335] the Panel included:

- The 1989 acquisition by Kreditanstalt für Wiederaufbau (KfW) of a 20% equity interest in Deutsche Airbus. The Panel held this transaction was a specific subsidy under Article 2 of the SCM Agreement and conferred a benefit to recipient under Article 1:1(b) of the Agreement because no private investor seeking a reasonable rate of return on its investment would have made the KfW acquisition at the time.

333. *See id.* paras. 957–958.
334. *See id.* paras. 959–960.
335. *See id.* paras. 12, 571(g), 1414(h).

- The 1992 sale by KfW of its 20% equity stake in Deutsche Airbus to the parent of Deutsche Airbus, Messerschmitt-Bölkow-Blohm GmbH (MBB). The Panel held that this transaction was a specific subsidy under Article 2 of the SCM Agreement and conferred a benefit to recipient under Article 1:1(b) of the Agreement because this sale was for considerably less than market value.
- Four equity infusions; namely, capital contributions by France and one by Crédit Lyonnais to Aérospatiale (i.e., Airbus) between 1987 and 1994.[336] The Panel found these were "specific" under Article 2 of the SCM Agreement and conferred a benefit to recipient under Article 1:1(b) of the Agreement because the decision by the French government and Crédit Lyonnais to invest in Airbus was inconsistent with the usual practice of private French investors at the time. In reaching this finding, the Panel applied Article 14(a) of the Agreement and asked whether such investors would have made the capital contributions based on the information that was available to them at the time.[337] That information included data and financial ratios concerning the performance of Aérospatiale in relation to other firms operating in the same lines of business (e.g., revenues, profits, orders, deliveries, backlog, and market share), future prospects of Aérospatiale and predictions for the long-term growth of the LCA industry.
- A fifth equity infusion, the 1998 transfer by the French government of its 45.76% equity interest in Dassault Aviation to Aérospatiale (i.e., Airbus).[338] Here again, the Panel found this transfer to be "specific" under Article 2 of the SCM Agreement and conferred a benefit to recipient under Article 1:1(b) of the Agreement because it departed from the usual practice of French investors at the time.

Under the third general category, "R&TD Measures,"[339] the Panel included:

- Grants under the Second, Third, Fourth, Fifth, and Sixth EC Framework Programs.[340]
- R&TD grants by France between 1986 and 2005.

336. *See id.* paras. 994–1012.

337. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 996–999.

338. *See id.* paras. 1013–1027.

339. *See id.* paras. 13, 571(e), 1414(f).

340. *See id.* paras. 13, 571(e), 937–952, 1414(f). Note that the Appellate Body agreed with the United States that the analysis of specificity need not occur at the aggregate level of Airbus and the aerospace sector because the EU organized this support under the EC Framework Programs. In effect, the bureaucratic organization of subsidy schemes is not relevant; what matters in applying the specificity test is substantive access to funding. *See id.* para. 947.

- Grants by Germany under the Aviation Research Program, or LuFo I, II, and III.
- Grants by the German regional governments of Bavaria, Bremen, and Hamburg.
- Loans from Spain under its PROFIT and PTA I and II Programs.
- Grants by the United Kingdom under CARAD, later the Aeronautics Research Programme.

Because the aforementioned measures were "specific," they were potentially actionable under Articles 5 and 6 of the SCM Agreement. However, as for the purchase and sale transactions involving KfW and MBB, the Panel held that when, in 1998, the German government settled the accumulated DM7.7 billion debt of Deutsche Airbus, the government did not confer a "benefit" on Airbus. Thus, said the Panel, the debt settlement was not a "subsidy."

On all such findings (save for the ones discussed below) the Appellate Body agreed. That is, the Appellate Body agreed with the American argument and Panel that the aforementioned disputed subsidies satisfied the specificity test of Articles 1 and 2 of the SCM Agreement and conferred a "benefit" under Article 1:1(b).

Thus, the Appellate Body rejected an assortment of EU arguments, including, first, that Article 1:1(a)(1)(iii) of the SCM Agreement does not discipline the "creation" of infrastructure, but rather only its "provision."[341] Said the EU, "creating" infrastructure is by nature the establishment of general infrastructure, which is outside the ambit of this provision; only provision of a good or service to a recipient could incur discipline under the rule on infrastructure.

The Appellate Body said that the provision of infrastructure presumes as a precondition its creation and that nothing in Article 1:1(a)(1)(iii) excludes the possibility that creation of infrastructure is relevant to accurately characterizing what a government provided. In other words, there was no textual basis for the distinction the EU drew. Still, the Appellate Body modified the Panel ruling because of over-inclusive language.[342] Technically, Airbus got the Mühlenberger Loch site by a lease, so the city of Hamburg did not "create" the site. The city of Bremen did not "create" the exclusive right to use an extended runway with noise reduction features; rather, it furnished them to Airbus. Likewise, the ZAC Aéroconstellation site and lease of the EIG facilities were not created, as they were provided to Airbus.

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341. *See id.* paras. 961–968. Stylistically, it appeared that a different Appellate Body drafted different portions of the relevant text and e-mailed them to a central repository, with no careful editing thereafter. For example, paragraph 941 starts with "We," but the subsequent paragraphs (942–945) inexplicably change the person to "the Appellate Body"; i.e., from second to third person.

342. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 966–968.

Second, the Appellate Body denied that when evaluating the five capital contributions by the French government in Airbus, the Panel changed the standard set out in Article 14(a) of the Agreement for measuring "benefit" from these contributions.[343] That standard is whether government provision of equity constitutes an investment decision that is inconsistent with the usual investment practice of private investors in the WTO Member at issue. The EU said that the Panel paid lip service to this standard, but actually focused on whether the French government obtained a "reasonable rate of return." Not so, ruled the Appellate Body; the Panel did not establish or follow a distinct benchmark.

Given the rejection of these EU arguments, what were the exceptions? On which subsidy measures and associated legal points about the calculation of benefit did the EU enjoy a modicum of success on appeal? On the following controversial measures, the Appellate Body reversed or modified the holdings of the Panel:

- Infrastructure Measures[344]
  a) Assistance to Airbus to lease land at the Mühlenberger Loch industrial site in Hamburg.
  b) Lengthening of the runway at the Bremen Airport.
  c) The ZAC Aéroconstellation industrial site in Toulouse and associated EIB facilities.

The Appellate Body modified the characterization of the Panel that these three measures entailed a "financial contribution" under Article 1:1(a)(1)(iii) of the SCM Agreement (as noted above). Moreover, the Appellate Body reversed the finding of the Panel that they conferred a "benefit" under Article 1:1(b).

Why? The EU argued successfully that the Panel wrongly applied a "cost to government" standard in measuring the benefit to Airbus from infrastructure support. That is, the Panel held the essence of the benefit to Airbus from the infrastructure measures was that the cost of the investment in infrastructure by governmental authorities exceeded their return (generated by purchase or lease payments by Airbus) on that investment.[345] The EU said the return to the government approach of the Panel was the same as using a cost to government standard, which the Appellate rejected in the 1999 *Canada Aircraft* case.[346] Instead, said the EU, the Panel should have compared the returns to the government against the market value of the land or facilities sold or leased to Airbus, or the exclusive rights of use given to Airbus.

The Appellate Body agreed. Whether dubbed "return to government" or "cost to government," the approach of the Panel was wrong because it calculated "benefit" based on the investment costs that the relevant government authorities

343. *See id.* paras. 1000–1003.

344. *See id.* paras. 11, 571(f), 1414(f).

345. *See id.* para. 969.

346. *See* Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, paras. 150, 159–161,WT/DS70/AB/R (Aug. 2, 1999) (*adopted* Aug. 20, 1999).

incurred. The Panel should have determined "benefit" under Article 1:1(b) of the SCM Agreement with reference to the market.[347] That is, it should have asked whether the infrastructure support measures were financial contributions provided on terms more favorable than those available in the market.

But did the Appellate Body overturn the Panel ruling that the leased land at the Mühlenberger Loch industrial site in Hamburg and that the provision of the right to exclusive use of the extended runway at the Bremen Airport conferred a benefit on Airbus under Article 1:1(b)? Technically, yes. But the Appellate Body then went on to complete the analysis based on the findings of fact by the Panel and held that both measures conferred a benefit on Airbus:

> 989. . . . [T]he findings of the Panel establish a sufficient foundation for us to complete the analysis and determine that a benefit was conferred, even though we are not in a position to quantify that benefit. . . . [I]n order for the infrastructure associated with the Mühlenberger Loch site to have been provided for adequate remuneration, the value of a lease of that site to Airbus should have reflected the market value of the rental of comparable industrial land in Hamburg, plus a premium due to the contiguity and customization of that land for Airbus. However, because the Panel erroneously sought to assess the value of industrial land in Hamburg based on the amount the City of Hamburg invested in the development of the Mühlenberger Loch site, the Panel did not quantify that premium. *We nevertheless conclude, on the basis of the Panel's findings regarding the value of generally available industrial land in Hamburg and the location and customized features of the Mühlenberger Loch industrial site, that there was a certain premium that was not included in the rent that Airbus actually paid to lease industrial land at that site*.
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> . . . .
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> 992. Although the Panel did not consider that Airbus' payment of airport runway fees was relevant to its benefit analysis, it nevertheless concluded that Airbus paid no additional charges for its use of the extended runway, and that Airbus was therefore provided the right to exclusive use of the runway extension for no additional remuneration. As was the case in respect of the infrastructure at the Mühlenberger Loch site, the Panel did not consider it necessary to quantify the amount by which the market value for the use of the runway extension exceeded the fees paid by Airbus for that use. *We nevertheless conclude, on the basis of the Panel's finding that Airbus did not pay additional fees for its use of the extended runway, that*

347. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 983.

> *Airbus was provided the right to exclusive use of the extended runway for which it paid no additional remuneration. Accordingly, we find that the provision of the right to exclusive use of the extended runway at the Bremen airport conferred a benefit on Airbus within the meaning of Article 1.1(b) of the SCM Agreement.*[348]

In brief, the Mühlenberger Loch and Bremen Airport measures were "benefits," as the United States said, but the Appellate Body could not quantify them precisely. What about the ZAC Aéroconstellation industrial site in Toulouse—did it confer any benefit to Airbus? The Appellate Body said it did not have a basis on which to compare payments made by Airbus with the market value for the purchased land and facilities at this site. With insufficient facts, the Appellate Body said it could not complete the analysis as to whether this infrastructure measure conferred a benefit.

- Corporate Restructuring Measures
  a) The 1998 transfer by the French government of its 45.76% equity interest in Dassault Aviation to Aérospatiale (i.e., Airbus).

On this transfer of equity interest, the Appellate Body reversed the holding of the Panel that this transfer conferred a "benefit" to Aérospatiale within the language of Articles 1:1(b) and 14(a) of the SCM Agreement.[349] The Panel said it considered whether a private investor would have entered into this transaction, based on contemporaneously available information. In truth, held the Appellate Body, the Panel did not rigorously apply the precept of Article 14(a).

This provision requires correct and precise identification of the "investment decision" and, thereafter, consideration of the market benchmark and the timing of the comparison to the transaction. As the Appellate Body logically stated:

> Article 14(a) of the *SCM Agreement* focuses the inquiry on the "investment decision." This reflects an *ex ante* assessment of the equity investment, taking into account the costs and expected returns of the transaction as compared to the usual investment practice of private investors at the moment the decision to invest is undertaken. . . . [T]he focus of Article 14(a) on the "investment decision" is a critical step in the analysis because it identifies *what* is to be compared to the market benchmark, and *when* that comparison is to be situated.[350]

348. *Id.* paras. 989, 992 (emphasis added) (footnotes omitted).
349. *See id.* paras. 571(h), 1013–1027, 1414(i).
350. *Id.* para. 1019 (emphasis in original).

The Panel did not correctly identify the "investment decision" to be assessed in relation to the Article 14(a) market benchmark of the usual investment practice. Before the Panel, the United States said that no private investor would have entered into the deal because of the dire financial straits of Aérospatiale at the time and the fact that the French government lost control of Dassault in the deal with no offsetting gains that could have been expected from the subsequent sale of the shares of Aérospatiale-Mara. The Panel seemed to ignore these points. Instead, it blithely stated that Aérospatiale could not attract private capital. So the Appellate Body faulted the Panel for failing to consider the costs of the transaction, the value of the French loss of control in Dassault, and the expected returns from the consolidation of companies and subsequent public share offerings. Because the Panel did not investigate these facts, the Appellate Body said it lacked a sufficient factual basis to opine whether the transaction conferred a benefit on Aérospatiale.

Further, at the Panel stage, the United States did not score a complete victory on specificity. The Panel ruled that certain subsidies alleged by the United States to be "specific" were not under Articles 2:1(a) or (c). Contrary to American claims, the Panel said certain measures within the following four generic categories of support were generally available and thus not within the scope of the SCM Agreement:

1. Preferential lending.[351] While the twelve EIB loans were financial contributions (under Article 1:1(a)(i) of the SCM Agreement) that conferred a benefit (under Article 1:1(b)) to Airbus because they were offered at below-market interest rates, they were not specific to Airbus.
2. Certain infrastructure measures.[352] Three measures under the rubric of Infrastructure Support were financial contributions conferring benefits to Airbus but failed to meet the specificity test. These measures were:
   - French road improvements sponsored by the French government in connection with the ZAC Aéroconstellation industrial site.
   - The British £19.5 million given to Airbus UK for its operations in Broughton, Wales.
   - The grant from the government of Andalusia to Airbus in Puerto Santa Maria.
3. Corporate restructuring measures.[353] The 1998 forgiveness of DM7.7 billion of debt owed by Deutsche Airbus to the German government did not satisfy the test of being a specific subsidy under Articles 1 and 2 of the SCM Agreement. Rather, the EU showed that DM1.75 billion for which Germany agreed to settle the

351. *See id.* para. 10.
352. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 11 n.53.
353. *See id.* para. 12.

outstanding repayment obligation of Airbus was equal to the present value in 1998 of the indebtedness of Deutsche Airbus to Germany.

4. Certain R&TD measures. Like the aforementioned measures, certain R&TD grants by the United Kingdom Technology Program did not satisfy the specificity test. And the promise by Germany to Airbus for an R&TD grant under the LuFo III Program did not even meet the definitions of "financial contribution" and "benefit" because they were not separate and independent from any benefit Germany might have conferred via a future transfer of the promised money.

On all such findings, the Appellate Body agreed. Thus, with regard to these subsidies, the Appellate Body was not persuaded by American arguments that they satisfied the specificity test of Articles 1 and 2 of the SCM Agreement. Significantly, the EU got a win through the Panel finding that the United States failed to prove there existed (as of July 2005) a specific subsidy commitment by the EU or EU countries to provide Launch Aid to the A350. The Appellate Body agreed here, too.

d. Yellow Light Subsidies and Adverse Effects in the Form of Serious Prejudice (GATT Article XVI:1 and SCM Agreement Articles 5 and 6)[354]

1) Two-Step Versus Unitary Approach

Even if a subsidy is "specific" under SCM Agreement Articles 1 and 2, it is not necessarily actionable. It must not only confer a benefit on the recipient (here, Airbus), but it also must cause an adverse effect to a producer of a like product. Under Article 5 of the Agreement, the "adverse effect" can take the form of injury, nullification or impairment of benefits, or serious prejudice. The term "serious prejudice" is of course used in Articles 5(c) and 6 of the SCM Agreement and GATT Article XVI:1.

In considering whether serious prejudice exists under these provisions, some WTO panels have taken a two-step approach, while others have used a unitary analysis. Under a two-step approach, a panel asks first whether serious prejudice (e.g., in the form of displaced and lost sales) occurred as a factual matter. If it did, then in step two, the panel considers whether the challenged subsidies actually caused that serious prejudice. In other words, step one asks whether serious prejudice occurred in the relevant marketplace, and step two is a causation inquiry. In a unitary analysis, both questions are considered together—market phenomena and causal relationships. The Appellate Body described this analysis as a counterfactual one:

354. This discussion is drawn from *id.* paras. 2, 4, 14–15, 1105.

> [T]he counterfactual analysis entails comparing the actual market situation that is before the adjudicator with the market situation that would have existed in the absence of the challenged subsidies. This requires the adjudicator to undertake a modelling exercise as to what the market would look like in the absence of the subsidies. Such an exercise is a necessary part of the counterfactual approach.[355]

In its 2005 *Cotton* decision, the Appellate Body expressed a preference for the unitary approach, asserting it "has a sound conceptual foundation."[356] The reason for this preference is, as the Appellate Body explained:

> Our view remains that a unitary approach that uses a counterfactual will generally be the more appropriate approach to undertaking the assessment required under Article 6.3 of the *SCM Agreement*. . . . [I]t is difficult to understand the market phenomena described in the various subparagraphs of Article 6.3 in isolation from the challenged subsidies. Rather, consideration of the effects of the challenged subsidies is intrinsic to the identification of those market phenomena. Any attempt to identify one of the market phenomena in Article 6.3 without considering the subsidies at issue can only be preliminary in nature since Article 6.3 requires that the market phenomenon be the effect of the challenged subsidy. This also means that a two-step approach simply defers the core of the analysis to the second step. In other cases, the problem might be the opposite. By artificially leaving aside the question of whether the market phenomenon is the effect of the subsidy, one could overlook market phenomena that are in fact occurring.[357]

This explanation is unconvincing, as it is based on a false dichotomy. It presumes the two steps are entirely disconnected from one another. In truth, the first step is forward-looking, and the second step is backward-looking. Perhaps not surprisingly, therefore, in the *Airbus* case, the Panel used the two-step approach, saying that the American arguments about serious prejudice in the form of price suppression rendered that method "entirely appropriate."[358] Both the United States and the EU accepted the Panel's use of this methodology, so no issue concerning it was raised on appeal.

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355. *Id.* para. 1110.

356. *Id.* para. 1107 (quoting Appellate Body Report, *US – Upland Cotton*, *supra* note 234).

357. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1109 (footnote omitted).

358. *Id.* para. 1108 (quoting Panel Report, *EC – Airbus*, *supra* note 8, para. 7.1731).

2) Serious Prejudice

On appeal, the Appellate Body was faced with the question of whether the Panel correctly held that certain subsidies provided by the EU and governments of some EU countries to Airbus are illegal under Articles 5(c) and 6:3 of the SCM Agreement. The issue was one of first impression for the Appellate Body; never before had it examined claims of displacement under Article 6:3 of the Agreement. In brief, was the Panel correct that Yellow Light subsidies to Airbus caused "serious prejudice" to the United States? The Appellate Body responded "yes," thus upholding the Panel and handing the United States an important victory.

The Appellate Body said that the subsidies covered by the Appellate Body ruling were Launch Aid (Member State Financing) for every model of Airbus, corporate restructuring, and infrastructure measures. The relevant period of investigation for the adverse effects was 2001 to 2006. Simply put, the Appellate Body agreed with the American argument and Panel that the disputed subsidies, which satisfied the specificity test, caused adverse effects to the interests of the United States. In particular, they caused serious prejudice to the American LCA industry; i.e., to Boeing.

At the same time (as noted in Part II.C.3.a.), the Appellate Body excluded from its Articles 5(c) and 6 ruling certain measures within three categories of subsidy schemes. That gave a partial victory to the EU, as those schemes failed the specificity test.

The EU also scored a partial victory when the Panel held, and the Appellate Body agreed, that the United States failed to prove the existence of a "Launch Aid Programme" as an EU measure distinct from individual grants of Launch Aid.[359] The United States alleged that France, Germany, Spain, and the United Kingdom systematically, and in a concerted, coherent, and coordinated fashion, provided Launch Aid that was tantamount to an unwritten "program," a specific subsidy, as distinct from formal, documented individual Launch Aid measures.[360] The United States even dubbed it a "formal and institutionalized industrial policy."[361] However, the Appellate Body accepted the EU point that the United States failed to adduce any evidence other than individual Launch Aid loans to support the proposition that there was an unwritten "program"; i.e., a whole greater than the sum of the parts, which itself constituted a measure and which caused adverse effects.

The Appellate Body found no such overarching or underlying conspiracy, as it were, and thus no violation of Articles 1 and 2 of the SCM Agreement. Because the United States did not prove the existence of a distinct, unwritten measure, that outcome was a foregone conclusion, as the Appellate Body, like the Panel, could not properly understand the substance of the American argument. To be sure, the Appellate Body did not exclude unwritten programs

359. *See id.* para. 2.
360. *See id.* paras. 2, 572(a), 609.
361. *Id.* paras. 778. *See generally id.* paras. 779–796.

from the definition of a "measure" that could be challenged under a GATT-WTO agreement.[362]

What, exactly, was the serious prejudice to the United States?[363] The Panel uncovered four untoward effects to Boeing's interests during the 2001-to-2006 POI. The Appellate Body agreed on some aspects of the Panel rulings but not others. As indicated earlier, in reaching its findings, the Panel applied a two-step test under Articles 5(c) and 6(a)–(b), as follows:

- Step one: serious prejudice? Did serious prejudice in the form of displacement and/or lost sales, or threat thereof, from the subsidizing country and/or third countries occur?
- Step two: causation? If serious prejudice (as defined in step one) occurred, then was it the effect of the subsidies, namely, Launch Aid?

The Appellate Body did not take issue with this methodology (though it repeated nearly ad nauseam its preference for the unitary approach). Moreover, the Appellate Body held that both steps of the two-step test were satisfied: displacement occurred on certain LCA models and in certain markets, and the displacement was caused by Launch Aid. In reaching this conclusion, the Appellate Body upheld several Panel findings, though on two particular points, it reversed those findings. The Appellate Body recommended that the EU remove the adverse effects from the illegal subsidies, so as not to cause serious prejudice to the United States, or withdraw those subsidies entirely.

After another twenty-one tedious paragraphs spanning nearly ten more largely unenlightening pages,[364] the Appellate Body summarized the obvious; namely, "displacement" under Article 6:3(a)–(b) of the SCM Agreement means:

> [W]here a complainant puts forward a case based on the existence of displacement as a directly observable phenomenon and the panel opts to examine it under a two-step approach, as was done in this dispute, *displacement arises under Article 6.3(a) of the* SCM Agreement *where imports of a like product of the complaining Member are declining in the market of the subsidizing Member, and are being substituted by the subsidized product*. Similarly, *under Article 6.3(b), displacement arises where exports from the like product of the complaining Member are declining in the third country market concerned, and are being substituted by exports of the subsidized product*. . . . [D]isplacement must be discernible. The identification of displacement under this approach should focus on trends in the

362. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 792.
363. *See id.* paras. 4, 14–15.
364. *See id.* paras. 1151–1172.

> markets, looking at both volumes and market shares. *The trend has to be clearly identifiable and an assessment based on a static comparison of the situation of the subsidized product and the like product at the beginning and at the end of the reference period would be inadequate*. Where a two-step approach is used under Article 6.3(a) and (b), and displacement has been shown on a preliminary basis, the complaining Member will have to establish, in addition, that such displacement is the effect of the challenged subsidies.[365]

Obviously, displacement of exports from the market of the subsidizing country (e.g., displacement of Boeing aircraft sales in the EU in favor of Airbus) violates Article 6:3(a) of the SCM Agreement. Displacement of exports from the market of another country (e.g., displacement of Boeing aircraft sales in China, in favor of Airbus) violates Article 6:3(b) of the Agreement. Applying this meaning to the facts at hand, the Appellate Body agreed with the Panel that disputed Airbus subsidies caused displacement of exports from the United States of certain models of Boeing aircraft from the EU and third-country markets.

In particular, said the Appellate Body, the subsidies caused displacement of exports of single-aisle and twin-aisle Boeing LCA to the EU, China, and Korea during the reference period of 2001 to 2006.[366] They also resulted in displaced exports of single-aisle Boeing aircraft from Australia during this POI.[367] The key pieces of evidence for such displacement were data on market share:

- In the EU, the market share of Boeing in twin-aisle LCA declined from 2001 to 2006. In the single-aisle LCA market, its market share was steady between 2001 and 2004, but then declined in 2005 and 2006.[368]
- In Australia, the dominant market position held by Boeing in the single-aisle LCA product market eroded during the POI.[369] Its market share increased from 50% to 75% between 2005 and 2006, but those shares were well below the levels Boeing hit between 2001 and 2003. As for twin-aisle aircraft, Boeing made no sales in Australia during the reference period.

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365. *Id.* para. 1170 (emphasis added).

366. *See id.* paras. 1181–1206, 1414(l), 1414(m)(ii)–(iii), 1414(p). In addition to single- and twin-aisle LCA, the Appellate Body considered a third product market: very large aircraft. However, for such aircraft, Boeing was the sole supplier during the reference period in several of the geographic markets at issue. *See id.* paras. 1181, 1183, 1185, 1189, 1191, 1193, 1195, 1197.

367. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1184, 1414(l), 1414(m)(i), 1414(p).

368. *See id.* para. 1181.

369. *See id.* para. 1183.

- In China, the market share of Boeing in single-aisle LCA fell from 67% to 50% between 2001 and 2006, and in twin-aisle aircraft plunged from 100% to 11% during that period.[370]
- In Korea, in the single-aisle LCA market, Boeing lost market share throughout the POI.[371] For twin-aisle LCA in 2001 and 2002, there was a split of two-thirds of the market for Boeing and one-third for Airbus. That percentage split became 50%-50% in 2003, 2004, and 2006 (and 60% to 40% in 2005).

Obviously, in the EU and third-country markets, Airbus aircraft took the position of the displaced Boeing planes.

Certainly, the Appellate Body did not agree wholeheartedly with all of the Panel's conclusions on displacement. Two in particular were problematic. First, to reach its conclusion that sales of Airbus aircraft displaced those of Boeing in both the EU and third-country markets and thus represented a form of serious prejudice under Article 5(c) of the SCM Agreement, the Panel had to interpret the terms "market" and "like product" as they are used in Article 6:3(a)–(b), which identifies potential types of serious prejudice for purposes of Article 5(c).[372] The Panel took the easy path: it simply defined one single market and one like product; namely, LCA. That is, the Panel assessed displacement of Boeing aircraft sales on the basis of a single subsidized product encompassing all Airbus models and a single product market for LCA.

That was too easy, or rather, too simplistic, said the Appellate Body, reversing the Panel's "single product market finding."[373] The Panel simply relied on the American characterization of the "market," "like product," and, therefore, the "subsidized product." The Panel ought to have distinguished among different types of aircraft models and different LCA product markets. That is, the Panel should have provided its own, independent determination about these terms. Its failure to do so was a violation of DSU Article 11.

Had the Panel done so, it would have realized that the reality of displacement was more complex than it found. Whether Airbus aircraft displaced those of Boeing depended on the aircraft model type and market at issue. That is why, as just explained, the Appellate Body distinguished between single-aisle and twin-aisle LCA, and between the market of the subsidizing countries (i.e., the EU) and third countries (e.g., Australia, China, and Korea).

In particular, the Panel defined "market" and assessed "displacement" on the basis of a single subsidized product and a single product market for LCA.[374] That is, the Panel said there was a single product market in which all Airbus and Boeing LCA competed. But the Panel did not make its own independent

370. *See id.* para. 1185.
371. *See id.* para. 1191.
372. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 571(j).
373. *See id.* paras. 1124–1147.
374. *See id.* paras. 1112–1113.

assessment of the facts. Rather, the Panel accepted the American characterization of the terms "market" and "product."

Yet the Appellate Body said it was unable to complete the analysis to determine whether there was more than one LCA product market. The evidence was insufficient. Accordingly, the Appellate Body rejected the EU argument that there were four separate allegedly subsidized families (i.e., product groupings) or five separate products of Airbus LCA.[375] Significantly, while the EU said that the error of the Panel with respect to the "single product market" undermined the finding of the Panel concerning displacement, the EU did not argue that no displacement occurred. To the contrary, the EU admitted that there were uncontested data that displacement occurred under various approaches to the "product market." Consequently, the quarrel on appeal between the EU and United States revolved around the degree of competition across LCA models, especially as between the extremes of the product ranges of Airbus and Boeing.[376]

The Appellate Body did point out that from the text of Article 6:3(a)–(b), it is clear that the analysis of displacement or impedance of sales is geographically constrained to the territory of the subsidizing Member or any relevant third country. Potentially, this constraint may not be all that limiting, as the market for a product could be the world market. The analysis of products and markets is connected because the term "market" in Article 6:3 is used along with the term "like product." The latter is defined in footnote 46 of the SCM Agreement as "a product which is identical, *i.e.*, alike in all respects to the product under consideration, or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration." Thus, as the Appellate Body said, identity or close resemblance is one factor to consider when deciding whether products are "like" and, in turn, in the same product market.

The Appellate Body went on to point out that the scope of the "market" to be studied under Article 6:3(a)–(b) may vary from case to case, depending on the facts.[377] That scope may extend beyond "like products" defined according to the familiar GATT criteria of physical characteristics, end uses, and consumer preferences. Such criteria help establish whether two products are in the same market. But to decide whether two products create competitive constraints on one another (i.e., whether they are substitutes for one another), other factors concerning the demand- and supply-side substitutability (that is, whether consumers consider the products to be substitutes and whether manufacturers can switch production quickly and at low cost from one good to another) may be examined to see if two products are in a single market.

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375. *See id.* paras. 1113–1114.

376. *See id.* para. 1148. That said, one Appellate Body member essentially dissented, stating that it is logically incorrect to complete the analysis of displacement when it is not possible to complete the analysis of the relevant product market or markets. *See id.* paras. 1149, 1205.

377. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1120–1123.

A second area of disagreement between the Appellate Body and the Panel, and thus an occasion for reversal by the Appellate Body, concerned the exact markets in which displacement occurred. The Panel ruled that the disputed subsidies caused serious prejudice in the form of displacement of Boeing aircraft in the market of the subsidizing country, the EU, and in the third-country markets of Australia, Brazil, China, Mexico, Singapore, and Taiwan; and threatened displacement in India.

To reach its conclusion that Boeing LCA were displaced from the EU market, the Panel applied a two-step test under Article 6:3(a) of the SCM Agreement.[378] The Panel also used the two-step test to reach its finding that Boeing LCA were displaced under Article 6:3(b) from the third-country markets of Australia, Brazil, China, Korea, Mexico, Singapore, and Taiwan, and that a threat of displacement existed with respect to India.[379] The Appellate Body disagreed with respect to some of these markets and reversed these rulings. The Appellate Body said the evidence did not establish displacement during the 2001-to-2006 POI in Brazil, Mexico, Singapore, or Taiwan, nor of a threat of displacement in India.[380]

The United States alleged that Boeing lost out on sales of its planes to Airbus when Airbus launched spirited campaigns on behalf of certain types of aircraft that benefitted from subsidies.[381] In particular, said the United States, Boeing LCA lost out to the Airbus A320 on sales to Air Asia, Air Berlin, Czech Airlines, and easyJet.[382] Boeing LCA also lost out to the Airbus A340 to Iberia, South African Airways, and Thai Airways. And Boeing LCA lost out on sales to the Airbus A380 to Emirates, Qantas, and Singapore airlines.[383] This result (lost sales), urged the United States, constituted a violation of Article 6:3(c) of the SCM Agreement.

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378. *See id.* para. 571(o)(i), (o)(iv).

379. *See id.* para. 571(l)–(m), (o)(i), (o)(iv).

380. *See id.* para. 1414(n). In particular, the Appellate Body found that market share data did not show a trend of Boeing losing market share to Airbus in four other third-country markets, Brazil, Mexico, Singapore, and Taiwan. In Brazil, the Appellate Body said that the data were insufficient to show Boeing losing market share to Airbus in either the single- or twin-aisle markets. *See id.* paras. 1189–1190. It rendered a similar finding with respect to the Mexican, Singaporean, and Taiwanese markets. *See id.* paras. 1193–1194, 1195–1196, 1197–1198. Generally speaking, in these third-country markets, the market share of Boeing in the single- and twin-aisle markets held steady. As for India, the Appellate Body said evidence on market share was insufficient to prove the American contention that Boeing was threatened with displacement. Indeed, Boeing gained market share in 2005 and 2006 in the single-aisle LCA market, and the decline in those years for the twin-aisle market was too sketchy a basis from which to infer a threat (especially given that there were no sales of twin-aisle LCA in 2001 to 2004). *See id.* paras. 1199–1202.

381. *See id.* paras. 1207–1228.

382. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 571(o)(ii).

383. *See id.* paras. 571(o)(ii)–(iii), 1219.

Interestingly, the evidence presented by the United States to support its allegation was anecdotal.[384] It consisted of media reports, press releases, and public disclosures by various airlines. These materials pointed to discounts offered by Airbus in competitive bidding against Boeing as being the reason Boeing lost out in the sales campaigns. The Panel agreed with the United States.

The Appellate Body upheld the findings of the Panel.[385] Citing the *New Shorter Oxford English Dictionary*, the Appellate Body defined "lost" (as in "lost sale") as a sale "that a supplier 'failed to obtain'" and pointed out that the adjective "significant" in Article 6.3(c) of the SCM Agreement modifies all three relevant phrases—"lost sales," "price suppression," and "price depression."[386] Accordingly, the Appellate Body explained how to discern the existence of "lost sales" under the two-step and unitary approaches:

> To summarize, we consider that, under Article 6.3(c), "lost sales" are sales that suppliers of the complaining Member "failed to obtain" and that instead were won by suppliers of the respondent Member. It is a relational concept and its assessment requires consideration of the behaviour of both the subsidized firm(s), which must have won the sales, and the competing firm(s), which allegedly lost the sales. The assessment can focus on a specific sales campaign when such an approach is appropriate given the particular characteristics of the market or it may look more broadly at aggregate sales in the market. The complainant must show that the lost sales are significant to succeed in its claim. Where lost sales are assessed under a two-step approach such as the one adopted by the Panel in this case, the finding of lost sales in the first step is necessarily preliminary and of limited significance in coming to a conclusion under Article 6.3(c). Similarly to the phenomena of displacement under Article 6.3(a) and (b), a definitive determination under Article 6.3(c) must await consideration of whether such lost sales are the effect of the challenged subsidy. While a two-step approach to the assessment of lost sales is permissible, in our view, the most appropriate approach to assess whether lost sales are the *effect* of the challenged subsidy is through a unitary counterfactual analysis. This would involve a comparison of the sales actually made by the competing firm(s) of the complaining Member with a counterfactual scenario in which the firm(s) of the respondent Member would not have received the challenged subsidies. There would be lost sales where the counterfactual analysis shows that, in the

384. *See id.* para. 1208.
385. *See id.* paras. 571(n), 1414(o).
386. *Id.* paras. 1214, 1215.

> absence of the challenged subsidy, sales won by the subsidized firm(s) of the respondent Member would have been made instead by the competing firm(s) of the complaining Member.[387]

Like the Panel before it, the Appellate Body rejected the EU contention that Boeing lost sales not because of subsidies to Airbus, but because of factors other than price.[388] Such factors included mismanagement of customer relations, fleet and route structure, political considerations, and technical specifications. This losing EU argument is noteworthy in that it shows the steps in the two-step approach are entirely separate from one another, as the Appellate Body essentially concedes in the above-quoted passage. A discussion of alternative causal factors sometimes arises in the context of the first step.

In the appeal, the principal point contested by the EU was whether sales by Airbus of the A380 to Emirates Airlines constituted lost sales of Boeing 747 LCA. The Panel said they did, and so, too, held the Appellate Body. That is, the Appellate Body said the Panel was correct in the first step of the Panel's two-step approach under Article 6:3(c) and thus in reaching the conclusion that sales of the A380 to Emirates Airlines constituted significant "lost sales," even though formal offers might not have been requested or made.[389]

3) Causation and Launch Aid Subsidies

Agreeing with the Panel, the Appellate Body found a "genuine and substantial" causal link between Launch Aid subsidies, on the one hand, and both displacement and lost sales, on the other.[390] This test—"a genuine and substantial relationship of cause and effect"—was the right one to apply under Articles 5(c) and 6:3(c) of the SCM Agreement, following the Appellate Body precedent in the 2005 *Cotton* case.[391] Additionally, as set out in the *Cotton* case, establishing a causal relationship means ensuring "the effects of other factors are not improperly

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387. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1220 (emphasis added).

388. *See id.* para. 1209.

389. *See id.* para. 1228. At the Panel stage, there also were arguments about another form of adverse effects from Launch Aid; namely, impediment and price suppression or depression under Articles 5(c) and 6:3(a)–(c) of the SCM Agreement. The United States contended that Launch Aid for each Airbus model impeded imports of Boeing LCA into the EU and also impeded exports of Boeing LCA from third counties, and that kind of import and export impediment violated Article 6:3(a)–(b) of the Agreement. The Panel disagreed, and the Appellate Body did not deal with the matter. *See* Panel Report, *EC – Airbus*, *supra* note 8, para. 8.4. The United States also urged that Launch Aid gave Airbus the financial flexibility to lower its prices. The consequence was significant price suppression and depression between 2001 and 2006, a violation of Article 6:3(c). Not so, said the Panel. *Id.* Here, too, the matter was not a principal topic of appeal.

390. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1300.

391. *Id.* para. 1232 (quoting Appellate Body Report, *US – Upland Cotton*, *supra* note 234, para. 438).

attributed to the challenged subsidies"; i.e., non-attribution is a key part of proving causation.[392] In proving causation, a "but for" evaluation may be helpful, as long as it is accompanied by a non-attribution analysis:

> The Appellate Body has said [in its 2008 *Cotton* compliance decision at paragraphs 374–375] . . . it may be possible to assess whether the particular market phenomena are the effect of the subsidies by recourse to a "but for" approach. Thus, one possible approach to the assessment of causation is an inquiry that seeks to identify what would have occurred "but for" the subsidies. In some circumstances, a determination that the market phenomena captured by Article 6:3 of the *SCM Agreement* would not have occurred "but for" the challenged subsidies will suffice to establish causation. This is because, in some circumstances, the "but for" analysis will show that the subsidy is both a necessary cause of the market phenomenon *and* a substantial cause. It is not required that the "but for" analysis establish that the challenged subsidies are a sufficient cause of the market phenomenon provided that it shows a genuine and substantial relationship of cause and effect. However, there are circumstances in which a "but for" approach does not suffice. For example, where a necessary cause is too remote and other intervening causes substantially account for the market phenomenon. This example underscores the importance of carrying out a proper non-attribution analysis.[393]

The United States advanced a "product theory" of causation, under which it said Launch Aid impacted the ability of Airbus to create and market LCA that it otherwise could not have.[394] In other words, the United States used a "but for" test: the adverse effects to Boeing would not have occurred but for the subsidies to Airbus. Referring frequently to the "but for" causation test and examining competing reports submitted by the United States (the Dorman Report) and the EU (the Wachtel Report), the Panel essentially did, too.[395] The Panel also addressed non-attribution, examining alleged mismanagement of customer relations by Boeing, geopolitics, and the role of engine manufacturers in various sales campaigns.[396]

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392. *Id.* (citing Appellate Body Report, *US – Upland Cotton*, *supra* note 234, para. 437).

393. *Id.* para. 1233 (citing Appellate Body Report, *United States – Subsidies on Upland Cotton – Recourse to Article 21.5 of the DSU by Brazil*, paras. 374–375, WT/DS267/AB/RW (*adopted* June 20, 2008) [hereinafter *US – Upland Cotton* compliance]).

394. *Id.* para. 1243.

395. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1234, 1244–1257.

396. *Id.* paras. 1259–1300.

The essence of the EU argument about causation was that most of the contested Launch Aid subsidies were decades old and, therefore, could not be the cause of present serious injury to Boeing. Indeed:

> [T]he A300 and A310 were launched more than 30 years ago, that is, in 1969 and 1978 respectively. The first delivery of an A300 to a customer took place in 1974, while the A310 was first delivered to a customer and put in service in 1985. According to the European Union, German LA/MSF [Launch Aid] for these LCA models was fully disbursed by the end of 1988; LA/MSF provided by France was disbursed by 1986; and Spanish LA/MSF for the A300 and A310 was fully provided to CASA by the end of 1992.[397]

Moreover, pushing a counterfactual analysis, the EU argued that even without Launch Aid, Airbus could have built and sold the single-aisle A320 LCA with 100 to 200 seats and the twin-aisle A330 with 200 to 300 seats in 1987 and 1991, respectively, three or four years after Airbus actually produced and sold these LCA models.[398] The Aid might have accelerated the timeframe in which these models came to market, but did not change the outcome. That was because, said the EU, Airbus had gained technological experience, there was growing demand for these models, and Boeing had outdated products.

The EU argument was unsuccessful. The Appellate Body repeated its findings under Article 5 of the SCM Agreement; namely, that subsidies do have a life, that they may be amortized over time and eventually may be removed, and that their effects generally diminish over time and eventually come to an end with the passage of time.[399] The Appellate Body accepted the conclusions of the Panel; namely, that without subsidies, Airbus would not have achieved the market presence it did in the 2001-to-2006 POI, that Airbus would have been a much weaker aircraft manufacturer and produced an inferior product at less competitive prices without the subsidies, and that sales of Airbus LCA would have been much lower than they were without the subsidies.[400] Thus, said the Appellate Body, the Panel was correct in the second step of the two-step test: the effect of Launch Aid was displacement of market share of Boeing in favor of Airbus, and lost sales of Boeing in favor of Airbus to Air Asia, Air Berlin, Czech Airlines, easyJet, and Emirates, Qantas, and Singapore airlines.[401]

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397. *Id.* para. 1239 (footnotes omitted).

398. *See id.* para. 1274; s*ee generally id.* paras. 1275–1298 (The EU conceded that without subsidies, Airbus would not have launched the A300 and A310 in 1969 and 1978, respectively.).

399. *Id.* paras. 1236–1238.

400. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1270–1272.

401. *Id.* para. 1414(p).

The Appellate Body also upheld, with some criticism, the finding of the Panel that but for Launch Aid, Airbus could not have developed and introduced into the LCA market the A380 in 2000:

> [W]e do not find that the Panel acted inconsistently with Article 11 of the DSU [which requires the Panel to conduct an objective assessment of the facts] in finding that "either directly or indirectly, LA/MSF [Launch Aid] was a necessary precondition for Airbus' launch in 2000 of the A380." Although we consider the Panel to have fallen into error in speculating about an alleged "economic incentive" to overstate sales and in referring to *ex post* events in its assessment of the Airbus A380 business case, we do not consider that these deficiencies invalidate the Panel's conclusions in relation to Airbus' ability to launch the A380 in 2000 in the absence of LA/MSF. The Panel's ultimate conclusion that LA/MSF was a "necessary precondition" for Airbus' launch of the A380 in 2000 was based on multiple considerations, such as the A380 business case itself, evidence on Airbus' ability to fund the A380 in the absence of LA/MSF, and the financial and technological impact of LA/MSF provided in relation to previous models of Airbus LCA. . . . [B]ased on these multiple considerations, the Panel had a sufficiently objective basis for its ultimate finding that LA/MSF was a "necessary precondition" for the launch of the A380 in 2000. Accordingly, we uphold the Panel's finding that "either directly or indirectly, LA/MSF was a necessary precondition for the launch of the A380 in 2000."[402]

Regrettably, to reach this conclusion, the Appellate Body expended forty-nine paragraphs spanning roughly twenty pages.

4) Causation and Subsidies Other Than Launch Aid

The Panel held that subsidies other than Launch Aid caused displacement of Boeing LCA from the EU and various third-country markets.[403] That was a violation of Article 6:3(a)–(b) of the SCM Agreement. And, decided the Panel, those subsidies caused lost sales in contravention of Article 6:3(c). The Panel focused on corporate restructuring (especially equity infusions), infrastructure development (namely, the Mühlenberger Loch and Aéroconstellation industrial sites, Bremen Airport runway extension, and regional grants by German and Spanish authorities), and R&TD support (that is, the Second, Third, Fourth, Fifth,

402. *Id.* para. 1356.
403. *See id.* paras. 1358–1364; *see also* paras. 1365–1380.

and Sixth EC Framework Programs; the Spanish PROFIT and PTA program loans; and grants to Airbus from the British, French, and German central governments, and German subcentral governments). These measures complemented and supplemented the product effect of Launch Aid, in that they contributed to the ability of Airbus to develop and sell LCA models, thereby displacing Boeing in terms of market share and gaining sales at the expense of Boeing. In reaching these conclusions, the Panel aggregated the effects of the various subsidy schemes, declaring that their structure, design, and operation did not preclude consideration of their combined effects.

On appeal, the EU objected. Essentially, it argued that the Panel should have linked each specific subsidy scheme to the launch of a particular Airbus model. The Appellate Body checked the work of the Panel, and upheld it. That is, in applying step two of the two-step test, the Appellate Body examined whether the Panel properly distinguished between the effects of Launch Aid in causing serious prejudice, on the one hand, from the effects of the other types of subsidies in causing serious prejudice, on the other. It did, said the Appellate Body, agreeing with the Panel that the effects of Launch Aid in causing serious prejudice were complemented and supplemented by the infrastructure measures that were specific to Airbus and by the equity confusions that met the specificity test. But the Appellate Body reversed the finding of the Panel that the product effect of Launch Aid was complemented and supplemented by R&TD subsidies.[404]

So the Appellate Body affirmed that the equity infusions and infrastructure measures that were specific subsidies under Articles 1 and 2 of the SCM Agreement did indeed complement and supplement the product effect of Launch Aid, and thus caused serious prejudice to American interests under Articles 5(c) and 6:3(a)–(c) of the SCM Agreement.[405] Simply put, with respect to the subsidies the Appellate Body agreed were specific to Airbus, there was a genuine causal link between them and the success of Airbus vis-à-vis Boeing. Without these measures, Airbus would have been unable to develop LCA models and features thereof on the schedule that it did.[406]

Only on causation of displaced and lost sales by R&TD subsidies did the Appellate Body overturn the Panel holding.[407] The Appellate Body did not opine that the R&TD support had no such causal effect. Rather, it said the facts reviewed by the Panel showed only that such support helped Airbus with pre-competitive LCA development, but did not speak to the question of giving Airbus

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404. *See id.* paras. 571(p), 1414 (q)–(s).

405. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1381–1391 (concerning equity infusions), 1392–1400 (infrastructure measures), and 1410–1412 (summarizing the findings).

406. The United States also argued that Launch Aid, corporate restructuring, and infrastructure measures allowed Airbus to undercut the pricing of Boeing aircraft. Such price undercutting violated Article 6:3(c) of the SCM Agreement. *See id.* para. 4. However, neither the Panel nor the Appellate Body reached a definitive conclusion on price undercutting.

407. *Id.* paras. 1401–1409, 1411–1413.

a competitive advantage against Boeing in sales. More evidence was needed to prove that the R&TD support led to technologies incorporated into Airbus LCA models that made production of them more efficient or otherwise aided Airbus relative to Boeing.

In sum, the victory for the United States on Yellow Light subsidies was a solid one, albeit not total. For several models of Airbus aircraft, Launch Aid and certain corporate restructuring and infrastructure support measures that were specific to Airbus caused adverse effects. Those effects were serious prejudice; namely, displacement and lost sales. This victory was more than enough. Technically, the Americans needed to show only one kind of serious prejudice, not the full panoply of possibilities, and prove causation by only one or a few subsidies. In actuality, they showed the EU schemes for Airbus were riddled with illegalities.[408]

e. Red Light (Prohibited) Export Subsidies (SCM Agreement Article 3)[409]

1) Overview of Appellate Body Findings

There is no need to prove specificity with regard to Red Light subsidies. They are the most pernicious of subsidies because they directly aim to distort the pattern of trade. Once it is proved that a subsidy is contingent on exportation, in law or fact, it is irrebuttably deemed specific—and to cause an adverse trade effect. Thus, there is no need to show injury, nullification or impairment of benefits, or adverse effects concerning a prohibited subsidy. Obviously, from the perspective of any complainant, the best case scenario under the SCM Agreement is to prove the existence of a Red Light subsidy. That is what the United States sought to do with as many Airbus schemes as it could.

The key schemes targeted by the United States were seven types of Launch Aid contracts for the A330-200, A340-500/600, and A380, granted by the governments of Germany, Spain, and the United Kingdom. The United States alleged that these Launch Aid measures were, in fact, tied to anticipated exportation of the A380 and, therefore, were contingent in fact on export performance. Hence, on appeal, at issue was whether the Panel correctly held that

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408. The United States also failed to prove, at the Panel stage, that the challenged subsidies caused injury to the American LCA industry, in violation of Article 5(a) of the SCM Agreement. *See* Panel Report, *EC – Airbus*, *supra* note 8, para. 8.5(d). Because the United States did show serious prejudice, its defeat on showing injury did not alter the outcome of the case, as under Article 5 of the Agreement, the test for adverse effects is a three-pronged one (injury, nullification or impairment, or serious prejudice), with the prongs understood to be connected by the disjunctive ("or"; i.e., it is not necessary to prove all three prongs, just one).

409. This discussion is drawn from Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 2, 9, 1028–1104.

certain subsidies were prohibited under Article 3:1(a) and footnote 4 of the SCM Agreement, as de facto contingent on anticipated export performance. Article 3 is titled "Prohibition," and Article 3:1 states in part:

> 3.1. Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:
>
> (a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I.

Footnote 4 to Article 3:1(a) adds:

> This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.

Article 3:2 strictly prohibits subsidies (along with import substitutions under Article 1:1(b), which were not at issue in the case). The Appellate Body decided that the Panel incorrectly interpreted the above-quoted provisions, finding:

> 1102. . . . [T]he factual equivalent of *de jure* conditionality between the granting of a subsidy and anticipated exportation can be established where the granting of the subsidy is geared to induce the promotion of future export performance of the recipient. The standard for *de facto* export contingency under Article 3.1(a) and footnote 4 of the *SCM Agreement* would be met when the subsidy is granted so as to provide an incentive to the recipient to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy.
> . . . .
> 1103. . . . [T]he Panel equated the standard for *de facto* export contingency with a standard based on the reasons for granting a subsidy and that, in so doing, the Panel erroneously interpreted Article 3.1(a) and footnote 4 of the *SCM Agreement*. Because the Panel applied this erroneous standard in reaching its final conclusions, we therefore also *reverse* the Panel's conclusion . . . that "the United States has demonstrated that the German, Spanish, and UK A380 contracts amount to prohibited export

> subsidies within the meaning of Article 3.1(a) and footnote 4 of the *SCM Agreement*," and that "the United States has not shown that the granting of the . . . LA/MSF subsidies" by France for the A380, A340-500/600, and A330-200, and by Spain for the A340-500/600 "was contingent in fact upon anticipated export performance," within the meaning of Article 3.1(a) and footnote 4 of the *SCM Agreement*.[410]

Put succinctly, a subsidy may be de facto contingent on export performance if it is granted to induce better future export performance by the recipient; that is, to give the recipient an incentive to export beyond the normal conditions of market supply and demand. The Panel confused this standard of de facto export contingency with the reasons for granting a subsidy by equating them. Yet in reversing the Panel, the Appellate Body handed the EU an incomplete victory:

> [T]he Panel's factual findings and undisputed facts on the record do not provide a sufficient basis for us to determine whether the LA/MSF subsidies under the contracts at issue are granted so as to provide an incentive to Airbus to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of these subsidies. We are thus not able to complete the analysis and determine whether the LA/MSF subsidies under the contracts at issue are geared to induce the promotion of future export performance by Airbus. Therefore, we are unable to make a finding as to whether the granting of the LA/MSF subsidies under these contracts is in fact tied to anticipated exportation within the meaning of Article 3.1(a) and footnote 4 of the *SCM Agreement*.[411]

So the Appellate Body did not absolve the EU of providing Red Light subsidies to Airbus. It simply could not decide that question.[412] Thus, the Appellate Body overturned the recommendation of the Panel that the EU cancel its alleged prohibited Launch Aid subsidies for the A380 within ninety days.[413]

2) Panel Mistakes

To appreciate why the Appellate Body held what it held, it is necessary to understand what the Panel decided, and why. At both stages of litigation, the United States argued that Launch Aid for the development of the A330-200,

410. *Id.* paras. 1102–1103.
411. *Id.* para. 1104.
412. *See id.* para. 1101.
413. *Id.* paras. 1104, 1416(j).

A340-500/600, and A380 was a subsidy contingent in law or in fact on export performance, and thus violated Article 3:1(a) and footnote 4.[414] The Panel cited the precedent set by the Appellate Body in the 1999 case *Canada – Aircraft* and pointed out that the meaning of the key word "contingent" in Article 3:1 is "conditional" or "dependent" (i.e., "dependent for its existence on something else"). This same meaning applies to claims of de facto or de jure export contingency.[415] For cases of de facto contingency, footnote 4 speaks of "tied to actual or anticipated exportation or export earnings." Such "tying" refers to a limit or restrictions on the conditions under which the subsidy was granted.[416]

Thus, to make out a case for a de facto export subsidy, a complainant must show: 1) a subsidy was granted, and 2) the subsidy was tied to 3) actual or anticipated exportation or export earnings.

By "anticipated" exportation and earnings, the Panel meant the subsidizing government expects or foresees exportation or export earnings after granting the subsidy. That is, it grants the subsidy because of this expectancy or foreseeability. That means, said the Panel, more than simply showing that the

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414. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 2, 9, 1029–1101.

415. *See id.* paras. 1030, 1036.

416. Arguably, there is circularity in the definition of "tied to." Consider the Appellate Body explanation of its *Canada – Aircraft* precedent:

> The Appellate Body explained in *Canada – Aircraft* that the word "contingent" means "conditional" or "dependent for its existence on something else", and that the legal standard for export contingency expressed in Article 3.1(a) is the same for both *de jure* and *de facto* contingency. With regard to the standard for *de facto* export contingency set out in footnote 4, the Appellate Body noted that the ordinary meaning of the word "tie" in the first sentence of the footnote is to "limit or restrict as to . . . conditions". The Appellate Body thus found that to satisfy the standard for *de facto* export contingency "a relationship of conditionality or dependence" must be demonstrated between the subsidy and "actual or anticipated exportation or export earnings". The Appellate Body further observed that the meaning of the word "anticipated" under footnote 4 is "expected" and that "[w]hether exports were anticipated or 'expected' is to be gleaned from an examination of objective evidence." The Appellate Body stressed, however, that the use of this word does *not* transform the standard for "contingent . . . in fact" into a standard that is satisfied by merely ascertaining "expectations" of exports on the part of the granting authority. The Appellate Body explained that, although a subsidy "may well be granted in the knowledge, or with the anticipation, that exports will result", "that alone is not sufficient, because that alone is not proof that the granting of the subsidy is *tied to* the anticipation of exportation."

Id. para. 1037. In other words, "tied to" means conditionality or dependence on anticipated exportation or export earnings, but "conditionality" or "dependence" bespeaks a tie; namely, a limitation or restriction on the conditions for obtaining the subsidy.

government anticipated export performance. It means showing that it granted the subsidy because of that anticipated performance.[417] As the Appellate Body put it:

> [T]he Appellate Body emphasized [in the *Canada – Aircraft* case] that, under the second sentence of footnote 4, "merely knowing that a recipient's sales are export-oriented does not demonstrate, without more, that the granting of a subsidy is tied to actual or anticipated exports." Rather, "the export orientation of a recipient may be taken into account as *a* relevant fact, provided that it is one of several facts which are considered and is not the only fact supporting a finding."[418]

Accordingly, said the Panel in *Airbus*, the "total configuration of facts" surrounding the decision of a government granting a subsidy is to be examined, and no one fact is decisive. From this examination, an inference may (or may not) be drawn about finding contingency in fact.[419]

Agreeing with the United States, the Panel issued a split ruling on when a subsidy can be said to be de facto or de jure contingent on the anticipated performance of the subsidized merchandise. Essentially, the split was along the lines of the model of Airbus aircraft. Favoring the United States, the Panel said that Launch Aid from Germany, Spain, and the United Kingdom to support the A380 was a de facto subsidy contingent on export performance of the A380 and thus was a Red Light subsidy. The Panel agreed with the American argument concerning the A380, which at the time of the case had not come into service, that when deciding whether the granting of a subsidy is, in fact, tied to anticipated exportation, the subsidy must be granted because of, or on the condition of, anticipated exportation. However, the Panel rejected the American contention that the other four Launch Aid measures were contingent in fact on anticipated export performance, namely:

- French Launch Aid contract for the A330-320;
- French Launch Aid contract for the A340-500/600;
- French Launch Aid contract for the A380; and
- Spanish Launch Aid contract for the A340-500/600.

The Panel said that the French and Spanish governments did not grant these contracts because of, or on the condition of, anticipated exportation. Also, the Panel rebuffed the American claim that Launch Aid for the A330-200, A340-500/600, and A380 was de jure contingent on anticipated export performance. Finally, the Panel rejected the American contention that the other three major

417. *Id.* para. 1030.
418. *Id.* para. 1039.
419. Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 346, 1031.

categories of subsidies—EIB preferential loans, corporate restructuring measures, and infrastructure measures—were de facto or de jure prohibited export subsidies.

On what configuration of facts did the Panel render its decision on de facto contingency for some, but not all, of the Airbus LCA models? The Appellate Body summarized the Panel's findings:

> 1032. The Panel next turned to review the evidence in order to determine whether the United States had established that the LA/MSF subsidies at issue were contingent in fact upon anticipated export performance. The Panel found that the United States had submitted sufficient evidence to establish that, at the time the relevant member State governments concluded the LA/MSF contracts, they were fully aware that Airbus was a global company operating in a global market, and that the A380, A340-500/600, and A330-200 projects would involve Airbus selling most, if not all, of its production in export markets. The Panel then examined the evidence submitted by the United States on the contingent relationship between the subsidies at issue and anticipated export performance. In the Panel's view, it was clear from the repayment provisions of the contracts, the market forecasts, as well as certain HSBI [highly sensitive business information] (including Airbus' business case for the A380 and French and UK Governments' critical project appraisals), that achieving the level of sales needed fully to repay each loan would require Airbus to make a substantial amount of exports. Moreover, the Panel noted that, as the European Communities had explained, the member States expected that the loans granted under the LA/MSF would be fully repaid. Thus, the Panel concluded that the governments of these member States, in granting the loans, must have counted on Airbus selling a sufficient number of LCA so as to repay the loans and that such sales necessarily included a substantial number of exports. On this basis, the Panel found that:
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> > . . . . without being decisive, this evidence supports the view that the provision of LA/MSF on sales-dependent repayment terms was, at least in part, "conditional" or "dependent for its existence" upon the EC member States' anticipated exportation or export earnings.
>
> 1033. The Panel then turned to examine the additional evidence advanced by the United States in order to determine whether that evidence "corroborate[d]" the alleged tie between the

> granting of the subsidies and anticipated exportation. Such additional evidence included other provisions in the LA/MSF contracts, representations made by Airbus in its application for the German LA/MSF measure, statements by government officials of the United Kingdom and France, as well as information from the French Government's critical project appraisals. On this basis, the Panel found that, with respect to the LA/MSF contracts for the A380 by Germany, Spain, and the United Kingdom, the relevant evidence demonstrated that the granting of the subsidies under these contracts was contingent in fact upon anticipated export performance. In contrast, with respect to the French LA/MSF contracts for the A380, A340-500/600, and A330-200 and the Spanish LA/MSF contract for the A340-500/600, the Panel found that the additional evidence did not add any support to the United States' claim beyond what was already indicated by the repayment provisions. Thus, the Panel concluded that the United States failed to establish that the granting of subsidies pursuant to these LA/MSF contracts was contingent in fact upon anticipated export performance.[420]

The Appellate Body took a different view from the United States and the Panel.[421]

3) Correct Test for De Facto Export Contingency: Distorting Market Supply and Demand Incentives

The EU and the United States did not doubt that the legal standard for de facto export contingency requires some kind of relationship between a subsidy and exportation. The question was the nature of that relationship: what must a claimant demonstrate to prove a subsidy is, in fact, tied to anticipated exportation? The United States believed that the Panel correctly answered this question. The EU argued that the Panel got the standard under Article 3:1(a) and footnote 4 wrong. The Panel created a "dependent motivation test," said the EU, whereby de facto export contingency can be shown simply by showing the government anticipated exports and that because of its anticipation of exports, it granted the subsidy. The EU called this test "dependent motivation," because the Panel looked at the dependency on anticipated exportation and then inquired whether the motivation for the subsidy was because of that anticipation.[422]

After a rather mind-numbing discussion of the meaning of the words "anticipated" and "expected" in paragraph 1043 of its Report, the Appellate Body came to the following insight:

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420. *Id.* paras. 1032–1033 (footnotes omitted).
421. *See id.* paras. 571(i), 572(b), 1414(j).
422. *Id.* paras. 1040, 1060.

1044. . . . Where a subsidy is alleged to be "in fact tied to . . . anticipated exportation", the relationship of conditionality is, unlike in the case of *de jure* export contingency, not expressly or by necessary implication provided in the terms of the relevant legal instrument granting the subsidy. Under such circumstances, we consider that *the factual equivalent of such conditionality can be established by recourse to the following test: is the granting of the subsidy geared to induce the promotion of future export performance by the recipient?*

1045. In reaching this interpretation of the standard for *de facto* export contingency under Article 3.1(a) and footnote 4 of the *SCM Agreement*, we do *not* suggest that the standard is met merely because the granting of the subsidy is designed to increase a recipient's production, even if the increased production is exported in whole. We also do *not* suggest that the fact that the granting of the subsidy may, in addition to increasing exports, *also* increase the recipient's domestic sales would prevent a finding of *de facto* export contingency. Rather, *we consider that the standard for* de facto *export contingency under Article 3.1(a) and footnote 4 of the* SCM Agreement *would be met when the subsidy is granted so as to provide an incentive to the recipient to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy*.

1046. The existence of *de facto* export contingency, as set out above, "must be *inferred* from the total configuration of the facts constituting and surrounding the granting of the subsidy", which *may include the following factors*: (i) the *design and structure* of the measure granting the subsidy; (ii) the *modalities of operation* set out in such a measure; and (iii) the relevant factual circumstances surrounding the granting of the subsidy that provide the *context* for understanding the measure's design, structure, and modalities of operation.

1047. Moreover, where relevant evidence exists, the assessment could be based on a comparison between, on the one hand, the ratio of *anticipated* export and domestic sales of the subsidized product that would come about in consequence of the granting of the subsidy, and, on the other hand, the situation in the absence of the subsidy. The situation in the absence of the subsidy may be understood on the basis of historical sales of the same product by the recipient in the domestic and export

> markets before the subsidy was granted. In the event that there are no historical data untainted by the subsidy, or the subsidized product is a new product for which no historical data exists, the comparison could be made with the performance that a profit-maximizing firm would hypothetically be expected to achieve in the export and domestic markets in the absence of the subsidy. *Where the evidence shows, all other things being equal, that the granting of the subsidy provides an incentive to skew anticipated sales towards exports, in comparison with the historical performance of the recipient or the hypothetical performance of a profit-maximizing firm in the absence of the subsidy, this would be an indication that the granting of the subsidy is in fact tied to anticipated exportation within the meaning of Article 3.1(a) and footnote 4 of the* SCM Agreement.[423]

In brief, the test for de facto export contingency is a market-based one, akin to the test for "benefit" from a financial contribution: based on the total configuration of the facts (or what American lawyers call the "totality of the circumstances"); is the recipient encouraged to alter its pattern of domestic versus foreign sales for reasons other than normal market supply and demand factors?

The Appellate Body furnished a numerical example. Assume a subsidy is designed to assist the recipient in boosting future production by five units, and the ratio of the export to domestic sales of the recipient is 2:3.[424] The question is whether it is anticipated that the subsidy will change this ratio. If not, there is no tying of the subsidy to anticipated exportation. But suppose it is expected that the subsidy will cause the recipient to export more than two of its units; that is, at least three of them. Then the subsidy is designed to skew the future sales of the recipient in favor of exports (even if it also increases domestic sales), and it would be de facto contingent on exports:

> Export-contingent subsidies will indeed favour a recipient's export sales over its domestic sales. Nonetheless . . . the fact that the granting of the subsidy may *also* increase the recipient's domestic sales would not necessarily prevent a finding of *de facto* export contingency, so long as the measure is geared to induce a recipient to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy.[425]

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423. *Id.* paras. 1044–1046 (emphasis added on last sentences in paragraphs 1044–1045 and paragraphs 1046–1047) (footnotes omitted).

424. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1048.

425. *Id.* para. 1053 (emphasis added).

Actual effects are irrelevant—whether the subsidy changes the ratio of export sales does not matter; rather, what matters is whether it is anticipated that it will do so on the basis of information available to the government at the time the government provided the subsidy.[426]

Moreover, this market-based test is an objective one, claimed the Appellate Body. It does not depend on the subjective motivation or intent of the granting authority or on the reasons stated by that authority as to why it granted the subsidy. Objective facts—the total configuration of them—are the proper basis for an inference. In support of this interpretation, the Appellate Body pointed not only to the context provided to the phrase "tied to . . . anticipated exportation" in footnote 4 by the second sentence of that footnote, but also to the Illustrative List of Export Subsidies in Annex I to the SCM Agreement because a characteristic common to items (b) through (l) on that list is that they give an advantage to exported products over those destined for domestic consumption.[427]

Applying this understanding of the Article 3:1(a) and footnote 4 test, the Appellate Body took issue with the work of the Panel. The Panel used the word "because":

> 1062. . . . [C]ertain language used by the Panel shows that the standard it adopted deviates from what is required under Article 3.1(a) and footnote 4. Specifically, the Panel stated:
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> > In concluding that the reference to "anticipated exportation or export earnings" in footnote 4 means to consider that exports will take place before they actually do, or to envisage that exports may take place in the future, we are not saying that the required *contingency* between the granting of a subsidy and anticipated exportation or export earnings may be demonstrated by merely showing that a granting authority anticipated export performance. Rather, we are saying that the required contingency may be demonstrated where the subsidy was granted *because* the granting authority anticipated export performance.
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> . . . .
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> 1064. . . . [T]here might, or might not, be some overlap between the concept of the reasons for granting a subsidy and that of the motivation for granting a subsidy . . . . [T]he standard for *de facto* export contingency is not met simply by showing that

426. *See id.* para. 1049.
427. *See id.* paras. 1050–1051.

> anticipated exportation is the reason for granting the subsidy . . . . [Also,] the standard for *de facto* export contingency is not satisfied by the subjective motivation of the granting government to promote the future export performance of the recipient.
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> . . . .
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> 1067. In sum, we do not consider that the Panel erred in its interpretation of "anticipated exportation" under footnote 4 of the *SCM Agreement*. We also do not consider that the Panel's interpretation of the term "anticipated exportation" led to the imposition of an erroneous "dependent motivation" standard. However, *the Panel erroneously interpreted Article 3.1(a) and footnote 4 of the* SCM Agreement *by equating the standard for finding that the granting of a subsidy is in fact "tied to" anticipated exportation with a standard based on the reasons for granting a subsidy. . . . [T]o determine whether the granting of a subsidy is in fact tied to anticipated exportation, recourse may be had to the following test: Is the granting of the subsidy geared to induce the promotion of future export performance by the recipient?* The Panel's interpretation of the term "in fact tied to" under Article 3.1(a) and footnote 4 of the *SCM Agreement* is not consistent with this interpretation we set out above. We therefore *reverse* the Panel's interpretation that, in order to find that the granting of a subsidy is in fact tied to anticipated exportation, a subsidy must be granted *because* of anticipated export performance.
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> . . . .
>
> 1086. . . . *The standard for* de facto *export contingency under Article 3.1(a) and footnote 4 of the* SCM Agreement *would be met when the subsidy is granted so as to provide an incentive to the recipient to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy*.[428]

In brief, by using the word "because" and thereby delving into the messy questions of the reasons or motivations for granting a subsidy, the Panel wrongly equated the standard of de facto export contingency with the reason or reasons for granting a subsidy.[429] The Panel should have looked at whether Launch Aid contracts gave Airbus an incentive to export in a way that was not simply reflective of conditions of demand and supply in domestic and export markets for LCA vis-à-vis those conditions in the absence of a subsidy.[430] Consequently, the

428. *Id.* paras. 1062, 1064, 1067, 1086 (emphasis on *reverse* and *because* in paragraph 1067 original; other emphasis added).

429. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1063.

430. *See id.* para. 1104.

Appellate Body reversed the findings of the Panel that the United States successfully demonstrated that Launch Aid contracts for the A380 by the British, German, and Spanish governments were de facto Red Light subsidies. Likewise, it reversed the Panel's conclusion that the French A330-200, A340-500/600, and A380 contracts, and the Spanish A340-500/600 contracts were not contingent in fact on export performance.[431]

4) Applying the Correct Test to the Facts of Launch Aid

With the proper legal test for such contingency in mind, the Appellate Body turned to the question of whether the Panel was correct in finding that Airbus export performance was anticipated when the British, French, German, and Spanish governments granted the controversial Launch Aid subsidies.[432] The Appellate Body had to determine whether, in spite of the legally incorrect test used by the Panel, there were sufficient undisputed facts on the record to justify the Panel finding that the following Launch Aid contracts were, in fact, tied to anticipated exportation within the meaning of Article 3:1(a) and footnote 4 of the SCM Agreement:

- British, French, German, and Spanish Launch Aid contracts for the A380.
- French Launch Aid contracts for the A340-500/600 and A330-200.
- Spanish Launch Aid contracts for the A340-500/600.

In all three instances, the Appellate Body overturned the decision of the Panel. Under the proper test for a subsidy being "in fact tied to" anticipated exportation, the factual record was insufficient to sustain a ruling that Launch Aid was a de facto Red Light subsidy. Indeed, much of that record contained redacted data (e.g., concerning numbers of aircraft deliveries in the schedule of repayments for the Spanish A340-500/600 contract, leaving unclear the specific numbers of aircraft sales needed to repay Launch Aid under this loan contract on a per-sale basis).[433]

To be sure, the Appellate Body agreed with the Panel that there were facts to support the conclusion the EU and its member governments granted Airbus subsidies in anticipation of exportation. The Panel examined evidence concerning:[434]

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431. *See id.* para. 1083.

432. *See id.* paras. 1068–1101.

433. *See id.* paras. 1087–1089, 1104.

434. *See* Appellate Body Report, *EC – Airbus*, *supra* note 8, paras. 1078–1079, 1095–1096.

- Market forecasts of sales of Airbus LCA.
- Appraisals of projects financed through Launch Aid.
- Relevant decisions by the European Commission on state aid.
- A statement by British Prime Minister Tony Blair, a press release by the United Kingdom Department of Trade and Industry, and statements reportedly made by French Prime Minister Lionel Jospin.
- Orders received for Airbus LCA at the time Launch Aid contracts were awarded.
- Language in the preambles and provisions of the Launch Aid contracts.

From such evidence, the Panel was impressed by the following facts:[435]

- Half of the orders for the A340-500/600 and all of the orders for the A330-200 received when these subsidies were granted were export sales.
- Demand within the EU for the A380, A340-500/600, and A330-200 in the ten to twenty years following Launch Aid would account for no more than 30% of total demand.
- More than 80% of the sales of Airbus in the decade preceding the granting of Launch Aid contracts were export sales.

So too was the Appellate Body. From these facts, the Appellate Body agreed the Panel was right to conclude that governments were aware of the prospect that a substantial number of LCA developed with Launch Aid subsidies would be sold to airlines outside the EU. The EU and its member governments were "fully aware that Airbus was a global company operating in a global market," and the projects supported by Launch Aid would "involve Airbus selling much if not most of its production in export markets."[436] Hence, the test of "anticipated exportation or export earnings" under footnote 4 of the SCM Agreement was satisfied: the EU and Britain, France, Germany, and Spain expected that exportation and export earnings would result from the development of the various Airbus models.

But showing Launch Aid was granted in anticipation of export earnings, according to footnote 4 of the SCM Agreement, was not enough to condemn that Aid as a Red Light subsidy.[437] The sole fact that a company exports is not sufficient to justify a finding of de facto contingency.[438] So evidence about domestic or global market forecasts alone is not enough.

The rest of the test for a de facto Red Light subsidy comes from Article 3:1(a); namely, was the subsidy in question contingent in fact on exportation? In other words, was Launch Aid in actual practice tied to anticipated exportation?

435. *See id.* para. 1079.
436. *Id.* para. 1080.
437. *See id.* para. 1081.
438. *See id.* para. 1092.

Here again, the Panel goofed: it defined "tied to" as "because of" anticipated export performance, thus involving itself in matters of the motivation for or intention behind the aid, rather than focusing on whether the aid created an extra-market incentive beyond normal patterns of supply and demand in EU and foreign LCA markets.

The rest of that test, and what the Panel should have considered, is whether the subsidy in question (Launch Aid) was granted to give the recipient (Airbus) "an incentive to skew its future sales in favour of export sales."[439] As the Appellate Body put it:

> 1090. With respect to the French, German, Spanish, and UK A380 contracts and the French A340-500/600 and A330-200 contracts, the evidence examined by the Panel, including the market forecasts and the repayment schedules under these LA/MSF contracts, indicates the following: (i) the financing under the LA/MSF contracts is provided in exchange for the condition that it be repaid; (ii) pursuant to the repayment terms under the contracts, Airbus undertook the obligation to repay the loans, on a per-sale basis, over a specified number of sales of the subsidized aircraft; and (iii) the number of sales contemplated under the repayment provisions of the contracts involves a significant amount of export sales. The Panel concluded that "it is clear from various pieces of information that achieving the level of sales needed to fully repay each loan would require Airbus to make a substantial number of exports." On this basis, as well as the relevant market forecasts, the Panel found that "the EC member States, fully expecting to be repaid, must have held a high degree of certainty that the provision of LA/MSF would result in Airbus making those export sales."
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> 1091. The Panel's above findings thus establish that, at the time the LA/MSF subsidies were granted, the relevant member State governments anticipated a substantial number of export sales by Airbus in order to repay the LA/MSF subsidies granted under the French, German, Spanish, and UK A380 contracts and the French A340-500/600 and A330-200 contracts. *These findings merely establish "anticipated exportation" within the meaning of footnote 4 of the* SCM Agreement. *In order to demonstrate in addition that the granting of the subsidies under the LA/MSF contracts in question is "in fact tied", within the meaning of that footnote, to such anticipated exportation, it must also be shown that the granting of the LA/MSF subsidies is geared to induce the recipient to export in a way that is not simply*

439. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1092.

> *reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of these subsidies*. Yet the Panel's findings do *not* shed light on the question as to whether the fact that Airbus was anticipated to make a significant number of export sales under the LA/MSF contracts is not simply reflective of conditions of supply and demand undistorted by the granting of the subsidies.
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> . . . .
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> 1097. In sum, the Panel's findings on the basis of the additional evidence showed the reasons for the granting of the subsidies under the German, Spanish, and UK A380 contracts. However, . . . *the standard for finding that the granting of a subsidy is in fact tied to anticipated exportation is not met simply by showing that anticipated exportation is the reason for granting the subsidy*. . . . *[T]he reason for granting the subsidy is not the same thing as whether the granting of the subsidy is geared to induce the promotion of future export performance by the recipient*.
>
> 1098. Therefore, all of the above factual findings, taken together, still leave the following question unanswered: At what level would Airbus be anticipated to sell in the domestic and export markets *undistorted by the granting of the subsidies* under the LA/MSF contracts in question? Among the evidence examined by the Panel, the only piece that shows market conditions undistorted by the granting of the subsidies under the LA/MSF contracts at issue relates to the demand side, namely the projected demand for LCA by airlines worldwide. Such evidence gives no indications as to whether or how LA/MSF subsidies give an incentive to Airbus to skew its future sales towards exports. Although the evidence concerning repayment terms and relevant market forecasts gives some indication of the extent to which Airbus may be expected to export, it does not show the extent to which Airbus would be expected to export in the absence of the granting of these LA/MSF subsidies. Without such evidence, it is impossible to determine whether the LA/MSF subsidies were granted so as to induce Airbus to export a higher proportion of its production than it would otherwise, thereby giving Airbus an incentive to skew its future sales in favour of export sales. The Panel's factual findings and undisputed facts on the record, therefore, do not provide a sufficient basis for determining whether the LA/MSF subsidies under these contracts were granted so as to provide an incentive to the recipient to export in a way that is not simply reflective of

> the conditions of supply and demand in the domestic and export markets undistorted by the granting of these subsidies.[440]

So the Appellate Body ruled that Launch Aid from Germany, Spain, and the United Kingdom for the Airbus A380 was not contingent in fact on export performance and thus not a prohibited export subsidy.

5) Emphasizing the Distinction Between Granting a Subsidy in Anticipation of Exportation (Footnote 4) and De Facto Contingency on Exportation Based on Market Demand and Supply Distortions (Article 3:1(a))

To explain in greater detail, the Appellate Body said the Panel was wrong to hold that under Article 3:1(a) and footnote 4 of the SCM Agreement, when interpreting the terms "contingent," "tied to," "actual or anticipated," and "export performance," a subsidy will qualify as Red Light if that subsidy is granted merely because of actual or anticipated export performance:

> 1092. . . . [I]n Airbus' GMFs [Global Market Forecasts] reviewed by the Panel, the market forecasts for aircraft deliveries were based on an estimate of fleet development of airlines around the world, or of the regional distribution of global aircraft demand. For example, the GMFs issued in 1999 and 2000 predict, respectively, that demand by European airlines would represent 23% of total demand by airlines worldwide by 2018, and that, by 2019, demand by European airlines for "aircraft with more than 400 seats" would be 247 aircraft, or 20% of the worldwide demand. Such evidence, therefore, relates to only the existing condition of worldwide demand by airlines that was forecast at a level of 1,235 "aircraft with more than 400 seats." The fact that demand by non-European airlines was projected at 988 aircraft and demand by European airlines at 247 aircraft simply shows that Airbus is an export-oriented company. However, pursuant to the second sentence of footnote 4, the fact that a company exports, *alone*, is not a sufficient basis for finding *de facto* export contingency. . . .
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> 1094. The United States points out that, if Airbus had been required to repay over a lower level of deliveries, for example,

440. *Id.* paras. 1090–1091, 1097–1098 (emphasis original in paragraph 1098; other emphasis added) (footnotes omitted).

> lower than the projected 247 aircraft with more than 400 seats demanded by European airlines, export sales might not be *necessary* in order to fully repay the loan. Yet, in our view, it is likely that, among the aircraft sales projected for the European market, Boeing would supply a portion of that demand. Moreover . . . the GMF forecast of 1,235 sales globally and 247 sales in "Europe" is reflective of conditions of supply and demand in an industry that is highly export-oriented. Consequently, even under repayment terms that require Airbus to repay the LA/MSF over a considerably lower number of sales than 247 (because part of these sales will go to Boeing), Airbus would be expected to export a large part of its future production and would necessarily remain an export-oriented company. It is conceivable that existing conditions of supply and demand would lead to a higher proportion of domestic sales when production decreases or to a higher proportion of export sales when production increases. Yet nothing in the Panel's findings or undisputed facts on record show the level at which Airbus would be expected to sell in the domestic and export markets under a repayment term that requires it to repay the loans over a smaller number of sales. Thus, the Panel's factual findings and record evidence do not indicate to us whether the granting of LA/MSF subsidies is designed so as to give Airbus an incentive to skew its future sales in favour of export sales, thereby inducing the promotion of Airbus' future export performance.[441]

In other words, there was plenty of evidence to show that Airbus would make a substantial number of export sales, and in doing so, would repay the Launch Aid loans. But were those sales due to the global nature of the LCA market and the growing demand around the world for LCA?[442] Or were those sales due to the design and structure of the Aid, in that Airbus was expected to make a significant number of export sales above and beyond what relevant market supply and demand factors would dictate?

The United States showed that the British, German, and Spanish government contracts for the Airbus A380 subsidized the A380 because they granted the contracts based on anticipated exportation of that model. From that basis alone, said the United States and the Panel, the subsidy was prohibited as it was de facto contingent on actual or anticipated export performance.

The Appellate Body said the Panel used too narrow a basis from which to draw too grand an inference. A subsidy could be granted because of anticipated exportation, but ipso facto, that was not enough to hold the subsidy was de facto contingent and thereby Red Light. Rather, the proper test for de facto contingency

441. *Id.* paras. 1092, 1094 (emphasis in original) (footnotes omitted).
442. *See id.* para. 1093.

is whether a subsidy such as Launch Aid is "geared to induce the promotion of future export performance by the recipient."[443] So a complainant like the United States had to do more than assert that Launch Aid was granted because of anticipated exports; it had to show that the Aid was geared to promoting exports. To some degree, perhaps this distinction may seem to be one without much of a difference. But apparently the Appellate Body was attempting to set the bar higher than the Panel before categorizing a subsidy as Red Light.

5. Commentary

a. The Obvious Comment

The Appellate Body did not advance the cause of international jurisprudence by issuing a monstrously long report. To the contrary, its prolixity undermines its power. Filled with material that could be cut or slimmed down, such as paragraph 588 at pages 250 through 251, the Report invites even the seasoned international trade lawyer to do something else with her valuable time. (For the desperately curious, paragraph 588 covers which models of Airbus aircraft did not receive Launch Aid. But, by negative implication from paragraph 584 at pages 249–250, which identifies the models that did get the Aid, paragraph 588 is redundant.) How magnificent it would have been if, in such a brutally hard-fought case as this one, the Appellate Body would have issued a decision both curt and straightforward. But the Appellate Body members elected to issue a decision that is surprisingly simple on substantive matters.

Given its workload and need for translation of its decisions, the Appellate Body ought to have been pressed for time and thus issued a short report. But as any good writer knows, including the authors, who from time to time have probably been guilty of producing excessive pages, it takes longer to write less—the extra time being needed to think through the essential points and edit out clutter. Clutter is what much of the Appellate Body *Airbus* report is. For example, pages 16 to 237 are a regurgitation of the arguments of the parties and third parties. Much of the information in these 200-plus pages may well be available from the parties (via a website or a Freedom of Information Act-type request, if need be) or could be relegated to an annex to the report. Perhaps the Appellate Body members took the less time-consuming path of cutting and pasting large sections of different documents into one gargantuan decision.

Yet, in retrospect, is time really the culprit? The Panel was established in July 2005, and the Appellate Body circulated its report in May 2011, following circulation of the Panel Report in June 2010 and a notice of appeal from the EU in July 2010. Surely in the roughly five years available to the Panel, it need not have written about a page a day, but rather winnowed down issues and discussions to the essential ones. Similarly, in the approximately ten months available to the

443. *Id.* para. 1414(j).

Appellate Body, could it have eschewed writing about a page a day and considered more carefully use of Occam's Razor?

The dilated report is not only short on legal significance, but is also long on irritating ambiguities and inconsistencies, if not outright mistakes, all of which are the result of poor writing skills. For instance, consider the first sentence of paragraph 592 at page 252:

> The "1969 A300 Agreement" [between the France and Germany regarding Airbus A300 B] envisaged in general terms that the French and German Governments would provide a specified amount of funding for the development of the A300 in the form of loans to be repaid through a series of graduated levies on the sale of each aircraft, *the value of which* was expressly identified.[444]

The last clause, specifically the phrase "of which," is ambiguous. Does the 1969 Agreement expressly identify the value of the graduated levies? Or does it expressly identify the value of the aircraft? This kind of indeterminacy is unacceptable and is the object of correction in a first-year American law school legal writing class.

b. Inconsistent Standards?

It is hard to escape the conclusion that the Appellate Body interfered with the Panel's assessment of the facts, as to both the American and EU positions on project-specific risk premiums to measure the financial contribution associated with Launch Aid. The Appellate Body protested to the contrary, but in the context of reviewing the EU benchmark.[445] Suppose the Appellate Body had been exercising the standard of review known in American administrative law as *Chevron* deference.[446] Then, relying on *Chevron*, it might well have simply stated that although it disagreed with the Panel's financial analysis, that analysis was not unreasonable, and the Appellate Body was not going to substitute its judgment for that of the Panel.

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444. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 592 (emphasis added) (footnotes omitted). Footnote 1422 at the end of this sentence piles on facts, but does not sort out the ambiguity, stating, "Panel Report, para. 7.534 (referring to 1969 A300 Agreement, Articles 6 and 7). The total amount of funding identified in the Agreement was set on the basis of *conditions de prix* (price conditions) existing on 1 January 1968, and was subject to revision in the light of any evolution in the *conditions économiques générales* (general economic conditions) since 1 January 1968. (*Ibid.* (referring to 1969 A300 Agreement, Article 6))." The same imprecision appears in paragraph 594 with respect to the 1981 A310 Agreement.

445. *See id.* para. 898.

446. *See* Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984).

The Appellate Body did not do that when evaluating the risk premium the United States proposed. It displayed its disagreements with the analysis of the Panel, and then overturned it. But it did exercise such deference with respect to the risk premium the EU offered. It trotted out a litany of complaints against the Panel's financial critique of the EU figure, but then upheld the Panel analysis. As the Appellate Body itself admitted:

> [W]e have found that the *Panel did not make an objective assessment of the facts under Article 11 of the DSU when it determined that the project-specific risk premium proposed by the United States* constituted the minimum project-specific risk premium for the A300 and A310 projects, the external upper boundary of the range for the project-specific risk premium for the A320, A330/A340, A330-200, and A340-500/600 projects, and the internal upper boundary of the range for the project-specific risk premium determined for the A380 project. We have also found . . . aspects of the Panel's reasoning concerning the project-specific risk premium proposed by the European Communities to be inconsistent with Article 11 of the DSU. *However*, we *upheld* the Panel's conclusion that the European Communities' proposed project-specific risk premium understates the risk premium that a market operator would have reasonably demanded Airbus pay for financing on the same or similar terms as LA/MSF for the A380.[447]

Did the Appellate Body behave consistently, exercising *Chevron*-type deference in both instances, and simply decide that one ruling, but not the other, had to be overturned? Perhaps, but an affirmative answer might not square with the efforts of the Appellate Body to debunk the Panel's analysis of both the American and EU project-specific risk premium. It is not clear why both Panel rulings failed to merit upholding, or why both did not deserve to be overturned. What is the student of the work of the Appellate Body to make of this work? In particular, why trust its Wall Street skills over those of the Panel? That rhetorical question is precisely why reviewing courts are supposed to back off second-guessing intensive factual assessments by lower courts or administrative agencies on matters outside their expertise.

c. Shades of Marxism?

Few contemporary students of international trade law are introduced to the rudiments of the Marxist-Leninist critique of trade and the subsequent development of that critique by world systems theorists and dependency theorists.

447. Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 923 (emphasis added).

That is a shame because, as condemnable as the prescriptions are that follow from this critique, the critique itself is potent. That is, the cure it offers is hideous, but the diagnosis is thought-provoking.[448]

One element of that critique is that states become tools for large multinational corporations (MNCs), forming part of an unholy alliance with the military and elites in local countries. The dispute between Airbus and Boeing arguably fits this pattern. The champion of Airbus is the EU, which essentially owns Airbus. The champion of Boeing is the United States, which has close ties to the company. Both governments offer defense-related contracts to their companies. And both governments and companies have close ties to airlines in foreign countries, many of which are wholly or partly state-owned and to which they seek to sell their aircraft. Consider, then, what Marx and Lenin would say about the case were they alive and writing today.

d. Lowering the Legal Standard on Countervailing Pre-Privatization Subsidies?

It is worth pausing to appreciate that on this matter, the United States has argued consistently against high standards that would inhibit the imposition of countervailing duties against pre-privatization subsidies. In a number of cases,[449] the American legal position, based on Department of Commerce practice, has been to allow for such imposition without having to tie each particular pre-privatization subsidy to a recipient and trace the benefits of that subsidy through the privatization process. The Appellate Body generally has ruled against the United States in such cases. Yet the Appellate Body holding in the *Airbus* case on extinction of benefits might signal a lowering of the standard, along the lines of the American arguments in previous cases.

448. For a discussion of this critique, see RAJ BHALA, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE ch. 8, sec. II (3rd ed. 2008); Raj Bhala, *Marxist Origins of the "Anti-Third World" Claim*, 24 FORDHAM INT'L L.J. 132 (2000).

449. Several of these cases have been analyzed in previous WTO Case Reviews. *See, e.g.*, Raj Bhala & David A. Gantz, *WTO Case Review 2003*, 21 ARIZ. J. INT'L & COMP. L. 317, 368–92 (2004) (discussing Appellate Body Report, *US – Certain EC Products*, supra note 272); Raj Bhala & David A. Gantz, *WTO Case Review 2000*, 18 ARIZ. J. INT'L & COMP. L. 1, 63–74 (2001) (discussing Appellate Body Report, *US – Bismuth Steel*, *supra* note 272).

D. Trade Remedies: Anti-Dumping, Countervailing Duties, and Non-Market Economies

1. Citation

Appellate Body Report, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, WT/DS379/AB/R (March 11, 2011) (*adopted* March 25, 2011).

2. Introduction and Background

In 2008, China challenged various aspects of the United States's imposition of anti-dumping (AD) and countervailing duty (CVD) measures in four separate combined AD and CVD actions against China on circular-welded steel pipe, light-walled rectangular pipe and tube, laminated woven sacks, and off-the-road (OTR) tires, ultimately resulting in the instant Appellate Body Report.[450] Three of the issues considered in China's partially successful challenge go to the heart of the U.S. Department of Commerce's methodology for imposing countervailing duties on Non-Market Economy (NME) Members such as China (and Vietnam).

The key issues raised by China on appeal were, first, the extent of evidence and analysis required for the investigating authority to treat state-owned commercial banks (SOCBs) and state-owned enterprise (SOE) input suppliers as "public bodies" supplying benefits to enterprises and thus subject to countervailing duties under the SCM Agreement. Second, China challenged the DOC's use of non-national commercial lending rates to determine whether lending rates offered to enterprises were concessional and thus actionable subsidies. Third, China alleged that the methodology used by the DOC in imposing both anti-dumping and countervailing duties on the same imports resulted in "double counting" of remedies because a subsidization was effectively punished twice, once under the anti-dumping laws and again through the imposition of a countervailing duty.

In retrospect, the most significant threat to the DOC's methodology[451] relates to allegations that by imposing both AD and CVDs against NMEs, the

450. Request for the Establishment of a Panel by China, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, WT/DS379/2 (Dec. 12, 2008); Appellate Body Report, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, para. 1, WT/DS379/AB/R (Mar. 11, 2011) (*adopted* Mar. 25, 2011) [hereinafter Appellate Body Report, *US – AD/CVD (China)*].

451. Under U.S. law, the Department of Commerce also is addressing a parallel challenge in a circuit court decision determining that the DOC lacked legal authority to bring CVD actions against NMEs without explicit Congressional authorization. *See* GPX Int'l Tire Corp. v. United States, 666 F.3d 732, 745 (Fed. Cir. 2011); *see also infra* Commentary, Part II.D.5.

DOC is double counting in contravention of GATT 1994[452] and various provisions of the SCM Agreement. The GATT provides, "No product of the territory of any contracting party imported into the territory of any other contracting party shall be subject to both anti-dumping and countervailing duties to compensate for the same situation of dumping or export subsidization."[453] In theory at least, there is no potential double counting with regard to domestic subsidies because a domestic subsidy provided to an enterprise should benefit both domestic and export sales in the same manner.[454] However, this supposition is fallacious when the NME methodology is used.

The DOC generally avoids the double-counting problem in parallel AD/CVD actions against market economy nations by adjusting for the possible overlap of a benefit calculated as a result of a government export subsidy and sales at less than fair value (dumping) to the extent the dumping margins result from that same situation with a setoff in appropriate circumstances.[455] Avoidance is far more difficult in an NME situation where the differences between the effects of dumping and subsidization on exported goods are difficult to distinguish.[456] Avoidance is also complicated where the magnitude of dumping and the amount of benefit are not based on actual prices and commercial loan rates in the NME home market but on surrogate values from other jurisdictions so that the dumping margins presumably incorporate any domestic subsidies.

Although the legality of bringing CVDs against NMEs was not in question because of the language in China's accession agreement,[457] non-market economies have caused complications for investigating authorities seeking to impose countervailing duties over many decades, including double counting.[458] At the DOC, this problem did not arise before 2006. From 1984 until the mid-1990s, the DOC generally followed a practice of declining to pursue CVD cases against NME nations. Because the U.S. CVD law was silent on treatment of MNEs, the DOC also took the view that it had discretion as to whether the law should be applied to NMEs; until 2006, that policy required that that the CVD law

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452. *See* Thi Anh Nguyet Le & Hong Quy Mai, *Double Counting in the US Legislation Against Non-Market Economies: 'As Such' and 'As Applied' Analysis*, 7 MANCHESTER J. INT'L ECON. L. 71, 86–88 (2010).

453. GATT 1994, *supra* note 64, art. VI(5).

454. Typically, the benefit from a domestic subsidy is allocated by the DOC across all production, whether exported or sold domestically. An export subsidy by definition benefits exports alone. *See* SCM Agreement, *supra* note 245, art. 3.

455. *See* 19 U.S.C. § 1677a(c)(1)(C) (2012).

456. *See* Ross Denton, *The NME Rules of the EC's AD and Countervailing Duty Legislation*, 36 INT'L & COMP. L.Q. 198, 236 (1987) (analyzing the double-counting problem under DOC practice).

457. *See infra* Principal Issues on Appeal, Part II.D.3.

458. This and the following three paragraphs are adapted from Gantz, PRCBs, *supra* note 224, at 111–12. For a more detailed discussion of the double-counting issue, see Le & Mai, *supra* note 452, at 77–86; TODD B. TATELMAN, CONG. RESEARCH SERV., RL33976, UNITED STATES' TRADE REMEDY LAW AND NON-MARKET ECONOMIES: A LEGAL OVERVIEW 12 (2007), *available at* http://fpc.state.gov/documents/organization/84323.pdf.

should not apply to NMEs, a position that was upheld by a U.S. federal court in *Georgetown Steel Corp. v. United States*.[459] The essence of the DOC's rationale was that it was impossible to determine the extent to which a "bounty or grant" (the terminology used in U.S. law for subsidies at the time) existed because the government, rather than normal market forces, determined through central planning the costs of various inputs used in the production of goods. Accordingly, subsidies could not be distinguished from other directives and controls imposed by the government. The court in *Georgetown Steel* accepted the DOC's view of U.S. law, holding:

> Those statutes indicate that Congress intended that any selling by nonmarket economies at unreasonably low prices should be dealt with under the antidumping law. There is no indication in any of those statutes, or their legislative history, that Congress intended or understood that the countervailing duty law would apply.[460]

However, after publishing a notice of investigation beginning in 2006,[461] the DOC reversed its CVD abstention policy and initiated a CVD action against China. In the so-called *Georgetown Steel* memorandum that accompanied the DOC's determination in 2007,[462] the DOC justified its change in practice for China. In that memorandum, the DOC analyzed the rationale for excluding NMEs from CVD actions in the 1980s (continuing into the 1990s) and attempted to distinguish the current situation. The DOC noted that in 1984, it had concluded:

> [T]he nature of the Soviet-style economies in the mid-1980s made it impossible for the Department to apply the CVD law. To determine that a countervailable subsidy had been bestowed, the Department needed to establish that: (a) the NME government had bestowed a "bounty or grant" on a producer; and (b) that the bounty or grant was specific. The Soviet-style economies at the time made it impossible to apply these criteria because they were so integrated as to constitute, in essence, one large entity. In such a situation, subsidies could not be

459. Georgetown Steel Corp. v. United States, 801 F.2d 1308, 1309 (Fed. Cir. 1986).

460. *Id.* at 1316.

461. Notice of Investigation of Countervailing Duty Investigations: Coated Free Sheet Paper from the People's Republic of China, Indonesia and the Republic of Korea, 71 Fed. Reg. 68,546-01 (Nov. 27, 2006).

462. Memorandum from Shauna Lee-Alaia & Lawrence Norton, Office of Policy, Imp. Admin., to David M. Spooner, Assistant Sec'y Imp. Admin., Countervailing Duty Investigation of Coated Free Sheet Paper from the People's Republic of China – Whether the Analytical Elements of the *Georgetown Steel* Opinion Are Applicable to China's Present-Day Economy (Mar. 29, 2007), *available at* http://ia.ita.doc.gov/download/nme-sep-rates/prc-cfsp/china-cfs-georgetown-applicability.pdf.

> separated out from the amalgam of government directives and controls.[463]

According to the DOC, China in 2007 was different:

> The current nature of China's economy does not create these obstacles to applying the statute. As noted above, private industry now dominates many sectors of the Chinese economy, and entrepreneurship is flourishing. Foreign trading rights have been given to over 200,000 firms. Many business entities in present-day China are generally free to direct most aspects of their operations, and to respond to (albeit limited) market forces. The role of central planners is vastly smaller . . . .
>
> Given these developments, we believe that it is possible to determine whether the PRC Government has bestowed a benefit upon a Chinese producer (i.e., the subsidy can be identified and measured) and whether any such benefit is specific. Because we are capable of applying the necessary criteria in the CVD law, the Department's policy that gave rise to the *Georgetown Steel* litigation does not prevent us from concluding that the PRC Government has bestowed a countervailable subsidy upon a Chinese producer.[464]

Although it did not discuss the issue in detail, the DOC effectively assumed that it had sufficient discretion to apply CVDs to NMEs under applicable U.S. law and *Georgetown Steel*, despite the questionable nature of this assumption as indicated by the excerpt from *Georgetown Steel* quoted above. Thus, once it decided that a policy change with regard to China was warranted, the DOC asserted that it could reverse its policy without Congressional authorization, regardless of the resulting logical inconsistency whereby China was still treated as an NME for AD purposes.[465] In any event, the policy changed and has been consistently imposed in cases against China (and Vietnam) since that time. In response to the *GPX International* decision, legislation was quickly enacted to restore the DOC's authority to apply the CVD laws to NMEs.[466]

While *Coated Free Sheet Paper* was ultimately terminated for lack of a demonstration of material injury to U.S. producers, countervailing duties (at rates of up to 615%) were applied to imports of line pipe into the United States in a

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463. *Id.* at 9–10.

464. *Id.* at 10.

465. The Court of Appeals for the Federal Circuit disagreed; *see infra* Commentary, Part II.D.5.

466. Rossella Brevetti, *Countervailing Duties: President Signs Legislation Restoring Subsidy Remedy for Nonmarket Economies*, 29 INT'L TRADE REP. (BNA) 400 (Mar. 15, 2012). *See also* Commentary, Part II.D.5.c.

2008 determination.[467] At least eighty-five sets of simultaneous AD and CVD orders against China have been issued, with additional orders pending before the DOC.[468] Also, Congress has strongly urged the DOC to make the new NME/CVD policy applicable to all NMEs.[469]

For the DOC, there are obvious conceptual inconsistencies between the use of NME methodology in an anti-dumping case (relying on surrogates because various input costs in the home market are not based on market-determined prices) and the assertion that "private industry now dominates many sectors of the Chinese economy" with a much smaller role of government planners so that government subsidies can be accurately measured in a CVD action. Even though (as discussed in detail in Part II.D.4.c. of this Case Review) the DOC relies on surrogates to determine subsidy benchmarks for interest rates and factor inputs from SOEs, the DOC will not be able to continue to bring both CVD and AD cases against China unless its methodology is changed to address double counting. Additional pressure for change will arise when the provisions in China's accession agreement authorizing NME treatment for AD purposes expire at the end of 2016.[470]

3. Principal Issues on Appeal

As noted above, China challenged many aspects of the Panel's review of the DOC's methodology in determining the existence of countervailable subsidies in the administrative proceedings.[471] These included:

- Whether it was erroneous to interpret "public body" as meaning "any entity controlled by the government" where both SOE suppliers and SOCBs were "public entities" under the SCM Agreement;
- Whether the Panel had determined erroneously that U.S. treatment of de jure specificity requirements generally were inconsistent with Article 2.1(a) of the SCM Agreement and whether the Panel

467. *Dumping, Countervailing Duties: ITC Affirmative Injury Finding in Pipe Case Is First Time CVD Duties to Apply to China*, 25 INT'L TRADE REP. (BNA) 960 (June 26, 2008).

468. *See* U.S. INT'L TRADE COMM'N, ANTI-DUMPING AND COUNTERVAILING DUTY ORDERS IN PLACE AS OF JUNE 09, 2011, BY DATE OF ORDER (2011), *available at* http://info.usitc.gov/oinv/sunset.nsf/AllDocID/96DAF5A6C0C5290985256A0A004DEE7D?OpenDocument (last visited Sept. 22, 2012).

469. Amy Tsui, *Countervailing Duties: Commerce Announces Significant Shift, Applies CVD Law in Chinese Paper Case*, 24 INT'L TRADE REP. (BNA) 495 (Apr. 5, 2007).

470. *See* Accession of the People's Republic of China, pt. 1, para. 15(b), WT/L432 (Nov. 23, 2001) [hereinafter China's Accession Protocol]; *id.* pt. 1, para. 15(d) (permitting NME treatment for fifteen years from Dec. 11, 2001).

471. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 270.

misinterpreted Article 2.2 in its consideration of regional industry specificity;

- Whether the Panel, in considering benchmarks used to calculate benefits, misinterpreted Articles 14(d) and 14(b) of the SCM Agreement with regard to U.S. rejection of in-country private practices and Chinese interest rates as benchmarks and use of a proxy (out of country) benchmarks instead;
- Whether the Panel erred by failing to find that the United States acted inconsistently with Articles 19.3 and 19.4 of the SCM Agreement and Article VI:3 of GATT by "concurrently imposing anti-dumping duties calculated on the basis of its NME methodology and countervailing duties in the investigations at issue," or double counting;
- Whether the Panel failed to comply with its "objective assessment" obligations of Article 11 of the DSU; and
- If the Appellate Body finds that the United States acted inconsistently with various provisions of the SCM Agreement and GATT Article VI:3, whether the United States also acted inconsistently with Articles 10 and 32.1 of the SCM Agreement.

The first four issues have considerable significance for the methodology used by the DOC (and by administering authorities elsewhere) in managing CVD actions brought against NMEs such as China and Vietnam.

4. Holdings and Rationale

a. Demonstrating That SOEs and SOCBs Are "Public Bodies"

The DOC has followed a practice, in these and other cases involving alleged subsidies, of assuming that if a state-owned commercial bank or state-owned enterprise were owned and controlled by the government, it could be considered, without further inquiry, a "public body" under Article 1 of the SCM Agreement. Under such circumstances, the difference between the actual SOCB lending rates and those of "benchmark" commercial banks would be considered actionable subsidies to the extent that other requirements (such as specificity) of the SCM Agreement were met. Similarly, if an SOE is a "public body" to the extent that it supplies input materials to an enterprise at prices below the commercial benchmark prices for such materials, the difference is considered an actionable subsidy. If the SOCBs and SOEs are not public bodies, any concessional lending rates or below benchmark prices would not be actionable under the SCM Agreement. The Panel had defined the term "public body" as

"any entity controlled by a government."[472] The definition is crucial because Article 1 of the SCM Agreement states:

> For the purpose of this Agreement, a subsidy shall be deemed to exist if:
>
> (a)(1) there is a *financial contribution by a government or any public body* within the territory of a Member (referred to in this Agreement as "government"), i.e., where:
>
> (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);
> (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);[473]
> (iii) a government provides goods or services other than general infrastructure, or purchases goods;
> (iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments . . . .
>
> and
>
> (b) *a benefit is thereby conferred.*[474]

472. *Id.* para. 278.
473. The footnote, numbered 1, reads:

> In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.

474. SCM Agreement, *supra* note 245, art. 1.1 (emphasis added).

Thus, unless the entity is a public body, or part of a funding mechanism, the financial contribution does not meet the WTO definition of a subsidy. The Appellate Body, as is often the case, began by consulting the dictionary, noting that:

> The word "public" is defined, *inter alia*, as "of or pertaining to the people as a whole; belonging to, affecting or concerning the community or nation", as "carried out or made by or on behalf of the community as a whole", or as "authorized by or representing the community". The word "body" in the sense of an aggregate of individuals is defined as "an artificial person created by legal authority; a corporation; an officially constituted organization, an assembly, an institution, a society".[475]

However, this "broad range of potential meanings" indicated that further analysis was required, and the Appellate Body noted the commonality between "government" and "public body." Because the term "government" shares commonality with "public body," the former term necessarily "informs" the meaning of "public body"; "the essence of government is that it enjoys the effective power to regulate, control, or supervise individuals, or otherwise restrain their conduct, through the exercise of lawful authority."[476] The "performance of governmental functions, or the fact of being vested with, and exercising, the authority to perform such functions are core commonalities between government and public body."[477] Ultimately, "the context of Article 1.1(a)(1)(i)–(iii) and in particular subparagraph (ii) lends support to the proposition that a 'public body' in the sense of Article 1.1(a)(1) connotes an entity vested with certain governmental responsibilities, or exercising certain governmental authority."[478] Thus, the relationship between the terms "government" and "public body" suggests that the latter is necessarily a governmental entity in terms of responsibilities or authority.

After discussing the object and purpose of the SCM Agreement—increasing and improving GATT disciplines relating to subsidies and countervailing measures—the Appellate Body turned to possibly relevant rules of international law, as specified in Article 31(3)(c) of the Vienna Convention on the Law of Treaties.[479] China had suggested that certain provisions of the International Law Commission's (ICL) articles on Responsibility of States for

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475. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 285 (footnotes omitted) (quoting 1 SHORTER OXFORD ENGLISH DICTIONARY 261 (6th ed. 2007); 2 SHORTER OXFORD ENGLISH DICTIONARY 2394 (6th ed. 2007)).

476. *Id.* para. 290 (citing Appellate Body Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*, para. 97, WT/DS103/AB/R, WT/DS113/AB/R (Oct. 13, 1999) (*adopted* Oct. 27, 1999)).

477. *Id.*

478. *Id.* para. 296.

479. *Id.* paras. 304–306.

Internationally Wrongful Acts[480] provided evidence of international law relating to the attribution of acts to states, while the United States had asserted that the ILC articles were not an "agreement" and, in any event, made no reference to the SCM Agreement, although the United States acknowledged that some parts of the ILC articles might constitute customary international law.[481] The Appellate Body did not determine whether the ILC articles constitute customary international law, but decided that the ILC articles may properly be taken into account by the Panel and the Appellate Body "as one of several interpretative elements."[482]

The sharing of concepts between "government" and "public body" did not resolve whether a particular entity is a public body. Rather, "the precise contours and characteristics of a public body are bound to differ from entity to entity, State to State, and case to case," and analysis will demand "conducting a proper evaluation of the core features of the entity concerned, and its relationship with government in the narrow sense."[483] What does this mean in individual circumstances? It depends:

> In some cases, such as when a statute or other legal instrument expressly vests authority in the entity concerned, determining that such entity is a public body may be a straightforward exercise. In others, the picture may be more mixed, and the challenge more complex. . . . We do not, for example, consider that the absence of an express statutory delegation of authority necessarily precludes a determination that a particular entity is a public body. What matters is *whether* an entity is vested with authority to exercise governmental functions, rather than *how* that is achieved. There are many different ways in which government in the narrow sense could provide entities with authority. . . . We stress, however, that, apart from an express delegation of authority in a legal instrument, the existence of mere formal links between an entity and government in the narrow sense is unlikely to suffice to establish the necessary possession of governmental authority. Thus, for example, the mere fact that a government is the majority shareholder of an entity does not demonstrate that the government exercises meaningful control over the conduct of that entity, much less that the government has bestowed it with governmental

480. *Draft Articles on Responsibility of States for Internationally Wrongful Acts*, *in* REPORT OF THE INTERNATIONAL LAW COMMISSION ON THE WORK OF ITS FIFTY-THIRD SESSION, UN GAOR, 56th Sess., Supp. No. 10, at 43, UN Doc. A/56/10 (2001), *available at* www.un.org/law/ilc, under "texts, instruments, and reports," topic 9.6. The General Assembly took note of the articles for the first time in General Assembly Resolution 56/83 of Dec. 12, 2001.

481. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, paras. 305–310.

482. *Id.* para. 316.

483. *Id.* para. 317.

> authority. In some instances, however, where the evidence shows that the formal indicia of government control are manifold, and there is also evidence that such control has been exercised in a meaningful way, then such evidence may permit an inference that the entity concerned is exercising governmental authority.[484]

In short, there can be no presumption that an entity owned by the government is a "public body" under Article 1 of the SCM Agreement simply because of ownership, and the Panel's decision was thereby reversed. Rather, the investigating authority—the DOC, in this instance—must demonstrate that the "entity is vested with authority to exercise governmental functions."

How, then, does this analysis apply to the DOC's determinations that SOEs and SOCBs are "public entities" under the SCM Agreement? In the case of SOEs, China asserted that the DOC should have included in its analysis five factors: government ownership, government presence on the board of directors, government control over activities, pursuit of government policies, and whether the SOE was created by statute.[485] In the affected proceedings, the DOC focused solely on the first factor, majority government ownership.[486]

According to the Appellate Body, the authorities have a "duty to seek out relevant information and to evaluate it in an objective manner." It is clear that SOEs "are not part of the government in a narrow sense." Here, "the question is whether they are public bodies or private bodies."[487] This determination, the Appellate Body recognized, can be complex, "particularly where the same entity exhibits some characteristics that suggest it is a public body, and other characteristics that suggest it is a private body."[488] Still, evidence of government ownership is not conclusive. Rather, according to the Appellate Body, "this is not sufficient because evidence of government ownership, in itself, is not evidence of meaningful control of an entity by government and cannot, without more, serve as a basis for establishing that the entity is vested with authority to perform a governmental function. Accordingly, such evidence, alone, cannot support a finding that an entity is a public body."[489] Moreover, the burden is on the DOC to establish "that SOCBs in China constitute public entities."[490]

In contrast to the analysis of SOEs, the DOC's analysis of the status of SOCBs had been much broader, relying in part on an earlier, detailed analysis in a

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484. *Id.* para. 318.

485. *Id.* para. 343; Panel Report, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, para. 8.101, WT/DS379/R (Oct. 22, 2010) [hereinafter Panel Report, *US – AD/CVD (China)*].

486. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 346.

487. *Id.* paras. 344–345.

488. *Id.* para. 345.

489. *Id.* para. 346.

490. *Id.* para. 352.

separate DOC determination for *Coated Free Sheet Paper*.[491] With SOCBs, the Department of Commerce relied not only on ownership but also considered other factors, such as provisions in the Commercial Banking Law requiring banks to "carry out their loan business upon the needs of [the] national economy and the social development and under the guidance of State industrial policies," as well as evidence of inadequate risk management and the fact that "during [the] investigation the [DOC] did not receive the evidence necessary to document in a comprehensive manner the process by which loans were requested, granted and evaluated to the paper industry."[492] Other information considered by the DOC included a report from the Organization for Economic Cooperation and Development indicating that executives of SOCBs are appointed by the government and that those choices are influenced by the Communist Party.[493] None of this evidence was challenged by China.

On this basis, the Appellate Body concluded that "these considerations, taken together, demonstrate that the USDOC's public body determination with respect to SOCBs was supported by evidence on the record that these SOCBs exercise governmental functions on behalf of the Chinese government."[494]

b. Specificity Requirements Under the SCM Agreement

In one of the four proceedings, *US – Tyres*, the DOC had found that the subsidies to the industry were specific and thus were actionable under the SCM Agreement. China challenged the finding, but it was upheld.[495] Article 1.2 reads:

> A subsidy as defined in paragraph 1 shall be subject to the provisions of Part II [prohibited subsidies] or shall be subject to the provisions of Part III [actionable subsidies] or V [countervailing measures] only if such a subsidy is specific in accordance with the provisions of Article 2.

Specificity is also governed by Article 2.1, which provides:

> In order to determine whether a subsidy, as defined in paragraph 1 of Article 1, is specific to an enterprise or industry or group of enterprises or industries (referred to in this Agreement as

491. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 349 (citing *Issues and Decision Memorandum for the Final Determination in the Countervailing Duty Investigation of Coated Free Sheet from the People's Republic of China* (Panel Exhibit CHI-93) (the "CFS Paper Issues and Decision Memorandum") at 58–60).

492. *Id.* para. 349 (citing the CFS Paper Issues and Decision Memorandum at 59–60).

493. *Id.* para. 350.

494. *Id.* para. 355.

495. *Id.* para. 361.

> "certain enterprises") within the jurisdiction of the granting authority, the following principles shall apply:
>
> > (a) Where the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific.
> >
> > (b) Where the granting authority, or the legislation pursuant to which the granting authority operates, establishes objective criteria or conditions governing the eligibility for, and the amount of, a subsidy, specificity shall not exist, provided that the eligibility is automatic and that such criteria and conditions are strictly adhered to. The criteria or conditions must be clearly spelled out in law, regulation, or other official document, so as to be capable of verification.
> >
> > (c) If, notwithstanding any appearance of non-specificity resulting from the application of the principles laid down in subparagraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of a subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy. In applying this subparagraph, account shall be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority, as well as of the length of time during which the subsidy programme has been in operation.

The Appellate Body observed that the "chapeau" frames the central inquiry and the principles set out in subparagraphs (a)–(c) within an analytical framework, but cautioned that "the application of one . . . may not by itself be determinative in arriving at a conclusion that a particular subsidy is or is not specific."[496] Subparagraphs (a) and (b), according to the Appellate Body, focus not on whether a subsidy has been *granted* to certain enterprises, but whether it is *limited* to certain enterprises. Thus, the issue is one of eligibility, not whether the subsidy is

496. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 366.

actually received, and the determination must consider both of the principles set out in subparagraphs (a) and (b) if various indications point to both.[497]

With regard to subparagraph (c), the Appellate Body was aware that, despite the "notwithstanding any appearance of non-specificity" language, a subject may be "in fact" specific. In other words, even where de jure specificity is absent because the statute is neutral, de facto specificity exists when the effect of the provision is to provide benefits only to a certain industry or industry group. This determination requires an application of the factors set out in Article 2.1(c) as well as interpreting the three subparagraphs together.[498] The essence of China's appeal was based on the assertion, contrary to the Panel's finding, that there must be language in the statute that limits access to the financial contribution and benefits to specific enterprises. The United States countered that under the text of the subparagraph, there are "many ways in which access to a subsidy could be explicitly limited" and that both contribution and benefit did not have to be set out explicitly in order for there to be a finding of such limitation.[499]

The Appellate Body reiterated that the key issue is whether access to a financial contribution is limited; the relevant legal instrument would constitute such a limitation even if it is silent on the benefit. One necessarily leads to the other.[500] Assuming *arguendo* that such was the case with regard to the legal instrument, China challenged the DOC's finding of specific financial contributions to the off-the-road tire industry. The DOC's conclusion was based in significant part on language in China's 11th Five-Year Plan, which set out four categories of industry: encouraged, restricted, eliminated, and permitted. Advanced radial tires and related materials and equipment were determined by the DOC to be listed explicitly in the "encouraged" category and were thus eligible for certain loans.[501] The Panel did not find, and China did not demonstrate, that similar loans were available to enterprises in the "permitted" category under the five-year plan.[502] This was critical because the Panel had found that "all financial institutions are *required* to provide credit supports in compliance with economic principles" to firms in the "encouraged" category.[503] No financing was available for the "eliminated" category, although under certain circumstances, loans might be made available for the "restricted" category; the "permitted" category was effectively the all others category, with no specific provision for or against lending.[504]

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497. *See id.* paras. 368–369.

498. *See id.* para. 370.

499. *Id.* para. 375 (quoting Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 9.26 (quoting the United States' appellee's submission)).

500. *Id.* para. 377.

501. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 381.

502. *Id.* para. 385.

503. Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 9.59, subpara. 1 (emphasis added).

504. *See* Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 384.

The Panel had not found that enterprises in the "permitted" category were eligible to receive loans in the same manner as those in the "encouraged" category. Moreover, the financial industry regulations were silent on lending to the "permitted" category. For the Appellate Body, the Panel was thus correct in "considering that the policy lending provided for in China's central level planning documents was explicitly limited to the 'encouraged' projects/industries . . . ."[505] The Appellate Body then reviewed the Panel's analysis, in which the Panel agreed that the DOC had reasonably concluded that various central, provincial, and municipal government planning documents, including a "catalogue" of individual projects, provided explicitly for the development of the OTR tire industry and that the totality of the evidence before the Panel further supported the DOC's findings of specificity with regard to SOCB lending.[506]

While the Appellate Body was less than fully satisfied with the Panel's analysis, it decided that "ultimately, the Panel conducted a proper factual analysis based on the totality of evidence, at all levels of government, on which the USDOC supported its specificity determination." Accordingly, there was no legal error in the Panel's analysis, and the Appellate Body affirmed the Panel's conclusion that the DOC determination that SOCB lending to the tire industry was specific.[507]

The Panel also had found that the DOC's determination of regional specificity in the investigation of laminated woven sacks was inconsistent with Article 2 of the SCM Agreement. China appealed because it disagreed with the basis for the Panel's conclusions.[508] The issues relate to Article 2.2 of the SCM Agreement, which provides:

> A subsidy which is limited to certain enterprises located within a designated geographical region within the jurisdiction of the granting authority shall be specific. It is understood that the setting or change of generally applicable tax rates by all levels of government entitled to do so shall not be deemed to be a specific subsidy for the purposes of this Agreement.

China challenged the Panel's determinations that: a) a finding of specificity could be based solely on the fact that the financial contribution, rather than the subsidy, was limited geographically, and b) a "distinct regime" is relevant to the specificity determination under Article 2.2.[509]

With regard to the first element, the Appellate Body supported the Panel; in the Appellate Body's view, "the purpose of Article 2 of the *SCM Agreement* is not to identify the elements of the subsidy as set out in Article 1.1, but to establish

505. *Id.* para. 385.

506. *See id.* para. 388–390; Panel Report, *US – AD/CVD (China)*, *supra* note 485, paras. 9.47–9.52.

507. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 400.

508. *Id.* para. 403.

509. *Id.* para. 407.

whether the availability of the subsidy is limited *inter alia* by reason of the eligible recipients (Article 2.1(a)) or by reason of the geographical location of beneficiaries (Article 2.2)."[510]

As to the second claim, the Panel had faulted the DOC for failing to establish that the financial contribution (local land-use rights in an industrial park) was limited to a single investigated company under Article 2.2. However, the Panel had observed that should the DOC have inquired into whether a "unique regime" existed in the industrial park, this might have resulted in a finding of regional specificity.[511] This, China argued, was an erroneous endorsement of a particular interpretation of Article 2.2. The United States, in contrast, argued that the Panel had expressly stated that it was not making a factual finding and, consequently, the issue was not subject to appeal.[512] The Appellate Body agreed with the United States; it essentially rejected China's assessment of the Panel's statements and held that China had failed to establish any error on the part of the Panel.[513]

c. Calculation of Benefit Through the Use of Out-of-Country Benchmarks

Neither the SCM Agreement nor China's accession agreement preclude the lodging of CVD actions against NMEs, or even the use of special procedures not countenanced in CVD actions against market economies. Rather, both are explicitly contemplated in the accession agreement:

> In proceedings under . . . the SCM Agreement, when addressing subsidies described in Articles 14(a), 14(b), 14(c) and 14(d), relevant provisions of the SCM Agreement shall apply; *however, if there are special difficulties in that application, the importing WTO Member may then use methodologies for identifying and measuring the subsidy benefit which take into account the possibility that prevailing terms and conditions in China may not always be available as appropriate benchmarks.* In applying such methodologies, where practicable, the importing WTO Member should adjust such prevailing terms and conditions before considering the use of terms and conditions prevailing outside China.[514]

When administering authorities calculate the magnitude of subsidies in matters, they typically compare the rate provided by the government entity (such as a

510. *Id.* para. 413.
511. *Id.* paras. 416–417.
512. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, paras. 418–419.
513. *See id.* paras. 421–424.
514. China's Accession Protocol, *supra* note 470, pt. 1, para. 15(b).

bank) to the "commercial" rate for the same type of loan, with the latter termed the "benchmark" rate. Thus, the SCM Agreement provides:

> [A] loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts.[515]

Questions arise when commercial lenders in the Member state offering government loans do not exist in significant numbers and/or are not considered independent from government control. Under such circumstances, the investigating authority chooses, for comparison purposes, a benchmark rate from commercial rates in locations where the banks are believed to be independent of government control. In these cases, the DOC ignored any possible domestic banks as benchmarks and resorted instead to a "basket" of loan rates derived from commercial bank lending in comparable developing countries. The DOC also used foreign steel prices as the comparison base, rather than prices offered by a small number of private steel companies in China, to determine whether SOEs supplying steel to the enterprises under investigation were doing so at subsidized prices. China objected in both instances. The Appellate Body considered each separately.

1) Out-of-Country Benchmarks for Hot Rolled Steel

Specifically, the DOC, in the circular welded steel pipe and light walled rectangular pipe and tube investigations, had rejected as benchmarks the price of hot rolled steel provided by private sources in China because steel production by SOEs in China accounted for 96.1% of the Chinese steel market, a "significant portion of production." Instead, the DOC used as the comparison benchmark various world market steel prices as reported in a steel industry publication, *Steel Benchmarker*.[516] The Panel, relying on *US – Softwood Lumber IV*,[517] found "nothing in that report that would prohibit, *a priori*, a finding of market distortion, and a decision to depart from in-country private prices, where the only relevant evidence was that the government is the predominant supplier of the good."[518]

China argued before the Panel that the Appellate Body, in *US – Softwood Lumber IV*, could not have meant to establish a per se rule whereby whenever a

515. SCM Agreement, *supra* note 245, art. 14(b).

516. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 429.

517. Appellate Body Report, *United States – Investigation of the International Trade Commission in Softwood Lumber from Canada: Recourse to Article 21.5 of the DSU by Canada*, WT/DS277/AB/RW (Apr. 13, 2006) (*adopted* May 9, 2006).

518. Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 10.45.

government is the predominant supplier of a good, the investigating authority may rely on non-national prices as benchmarks. The Panel agreed, but also noted that a finding of market distortion could be based solely on evidence that the government was the predominant supplier. China appealed on the grounds that such determinations were to be made on a case-by-case basis relating to the particular facts of the investigation.[519] The United States defended the Panel, contending that it had properly interpreted Article 14(d) of the SCM Agreement when finding that prominent supplier status was sufficient to reject national benchmarks, without any need to find price distortion.[520] Article 14 of the SCM Agreement states in relevant part:

> For the purpose of Part V, any method used by the investigating authority to calculate the benefit to the recipient conferred pursuant to paragraph 1 of Article 1 shall be provided for in the national legislation or implementing regulations of the Member concerned and its application to each particular case shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines:
>
> . . . .
>
> > (d) the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).

Focusing on *US – Softwood Lumber IV*, the Appellate Body noted that in that report, the Appellate Body had asked whether the provision permits the use of a benchmark other than private prices in the country providing the subsidy and had "answered the question in the affirmative, albeit subject to a number of qualifications." The Appellate Body there believed that the exclusive use of national benchmarks would violate the purpose of Article 14 and of the SCM Agreement. Rather, the Appellate Body determined that "prices in the market of the country of provision are the primary, but not the exclusive, benchmark for calculating benefit."[521] Second, in *US – Softwood Lumber IV*, the Appellate Body

519. *Id.* paras. 10.40–10.41; Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, paras. 432–433.

520. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 434.

521. *Id.* para. 438 (citing Appellate Body Report, *US – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, para. 97,

had considered when investigating authorities were permitted to use a benchmark other than private prices in the country of provision and found that such circumstances were "very limited" when "those private prices are distorted, because of the predominant role of the government in the market as a provider of the same or similar goods."[522]

China had argued that the findings in *US – Softwood Lumber IV* mandated analysis by the investigating authority of factors other than the government's market share as evidence of price distortion in the market.[523] However, the Appellate Body noted that in that earlier case, the Appellate Body had distinguished between situations where the government is the "sole" provider and where it is the "predominant" provider, but reasoned that even if the government is only the predominant provider, it was "*likely* that it can affect through its own pricing strategy the prices of private providers for those goods."[524] This reasoning, according to the Appellate Body, excluded the application of a per se rule, but where the government is the "predominant" supplier, the investigating authority is not required to conduct the same level of analysis as when the government is only a "significant" supplier.[525] In what the Appellate Body said was consistent with *US – Softwood Lumber IV*, it also noted that predominance could refer to market power rather than exclusively to market share.[526]

Finally, the Appellate Body, affirming the Panel, stated the general rule:

> [W]e are of the view that an investigating authority may reject in-country private prices if it reaches the conclusion that these are too distorted due to the predominant participation of the government as a supplier in the market, thus rendering the comparison required under Article 14(d) of the *SCM Agreement* circular. It is, therefore, price distortion that would allow an investigating authority to reject in-country private prices, not the fact that the government is the predominant supplier *per se*. There may be cases, however, where the government's role as a provider of goods is so predominant that price distortion is likely and other evidence carries only limited weight. We emphasize, however, that price distortion must be established on a case-by-case basis and that an investigating authority cannot, based simply on a finding that the government is the predominant supplier of the relevant goods, refuse to consider

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WT/DS257/AB/R (Jan. 19, 2004) [hereinafter Appellate Body Report, *US – Softwood Lumber IV*]).

522. *Id.* para. 439 (quoting Appellate Body Report, *US – Softwood Lumber IV*, *supra* note 521, para. 103).

523. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 440.

524. *Id.* para. 442 (quoting Appellate Body Report, *US – Softwood Lumber IV*, *supra* note 521, para. 100) (emphasis added).

525. *Id.* para. 443.

526. *Id.* para. 444.

> evidence relating to factors other than government market share.[527]

The Appellate Body then turned to the specific question of the DOC's rejection of in-country steel prices in the circular-welded and light-walled rectangular pipe investigations. There, the Panel had received and considered evidence from both sides relating to the Chinese government's role in the hot rolled steel market, leading the Panel to conclude that the DOC had not applied a per se rule.[528] Nor, according to the Panel, had China demonstrated through its evidence that, despite the government's market share, "the market was functioning and prices were not distorted," meaning that the DOC had not acted inconsistently with Article 14(d) in rejecting in-country private prices as benchmarks.[529] Among the factors considered relevant by both the Panel and the Appellate Body was the fact that with the SOEs producing 96.1% of the domestic HRS market, most of the remaining portion of the market (3%) was taken up by imports, a share considered too small relative to domestic production to be used as a benchmark.[530]

The Appellate Body ultimately rejected China's contention that the DOC, by failing to give greater weight to factors other than market share, had acted inconsistently with Article 14(d). The Appellate Body noted:

> [W]ith 96.1 per cent market share, the position of the government in the market is much closer to a situation where the government is the sole supplier of the goods than to the situation where it is merely a significant supplier of the goods. This, in our view, makes it *likely* that the government as the predominant supplier has the market power to affect through its own pricing strategy the pricing by private providers for the same goods, and induce them to align with government prices.[531]

The Appellate Body also rejected China's assertion that the DOC had failed to adequately "receive and consider" evidence other than market share and that the Panel, by accepting the DOC's conclusion that such consideration had taken place, had failed to comply with its responsibilities under Article 11 of the DSU.[532]

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527. *Id.* para. 446.

528. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 449; Panel Report, *US – AD/CVD (China)*, *supra* note 485, paras. 10.55–10.56.

529. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 450.

530. *Id.* para. 451.

531. *Id.* para. 455.

532. *Id.* paras. 463–464. DSU Article 11 provides in pertinent part that "a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements . . . ." *See* DSU, *supra* note 3, at art. 11; *see also supra* note 310.

2) Use of External Proxy Interest Benchmarks: SCM Agreement Article 14(b)

The Panel found in Article 14(b) of the SCM Agreement "sufficient flexibility to permit the use of a proxy in place of observed rates in the country in question where no 'commercial' benchmark can be found."[533] The Panel further found that the benchmark actually used by the DOC was not inconsistent with Article 14(b).[534] China appealed both findings. The United States supported the Panel, contending that the Panel "properly interpreted Article 14(b) of the *SCM Agreement* as permitting the use of proxies, including loans denominated in a different currency."[535]

In the pipe, sacks, and tires investigations, the DOC had rejected interest rates on loans in China as benchmarks because of "pervasive government intervention in the banking sector, which created significant distortions, restricting and influencing even foreign banks within China." Instead, the DOC used as a proxy an external benchmark, "a regression-based methodology . . . based on inflation-adjusted interest rates of a group of countries with a gross national income ('GNI') similar to that of China . . . ."[536]

For the Panel, the "central question of legal interpretation . . . is whether, and if so under what circumstances, Article 14(b) of the SCM Agreement permits the rejection of in-country interest rates as benchmarks for government-provided loans."[537] China disagreed, contending that the principal question for the Panel was whether a comparable commercial loan could be obtained in the market and that, under Article 14(b), the "in country" versus "out of country" paradigm "does not arise."[538]

Article 14(b) of the SCM Agreement reads in pertinent part:

> [A] loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts.[539]

The Appellate Body began its analysis by considering the "constituent elements" of Article 14(b): "comparable," "commercial," and a "loan which the firm could actually obtain on the market." For a benchmark loan to be "comparable," it "should have as many elements as possible in common with the investigated

533. Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 10.130.
534. *Id.* para. 10.209.
535. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 469.
536. *Id.* para. 470.
537. Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 10.105.
538. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 472.
539. SCM Agreement, *supra* note 245, art. 14(b).

loan."[540] With regard to "commercial," the identity of the provider is not relevant; the concept of commercial is not inconsistent with provision of financial services by the government. However, the comparison between the investigated loan and a commercial loan determines whether a benefit has been conferred, and the term "commercial" is defined as "interested in a financial return."[541] This is in contrast to Article 14(d) (discussed in Part II.D.4.c.1. of this Case Review), which connects the relevant "market" to "the country of provision or purchase." With Article 14(b), no geographical or national scope is specified for the "market." Accordingly, all the "formalistic" requirements of Article 14(b) must be met.[542]

Still, despite the differences in the two subparagraphs, "there may also be under Article 14(b) limited circumstances where an excessively formalistic interpretation of this provision could frustrate its purpose and prevent the calculation of the benefit." Where loans are distorted by government intervention, the investigating authority should be able to use another benchmark, so long as that benchmark approximates "a comparable commercial loan which the firm could actually obtain in the market."[543] However, there is a hierarchy that the investigating authority must follow. If no identical or almost identical loan is available, the authority should first seek comparable commercial loans held by the same borrower, then similar loans to a comparable borrower, with appropriate adjustments to reflect differing dates, size, maturity, currency, structure, and credit risk. If the differences are so significant that they cannot be addressed through adjustment, as the Panel indicated, the authority "should be allowed to use proxies as benchmarks."[544]

The Appellate Body, after noting the use of the conditional tense in Article 14(b), opined that "[i]n the absence of an actual comparable commercial loan that is available on the market, an investigating authority should be allowed to use a proxy for what 'would' have been paid on a comparable commercial loan that 'could' have been obtained on the market."[545] However, the Appellate Body also cautioned that the further the investigating authority moves away from an identical or nearly identical loan as a benchmark, "the more adjustments will be necessary to ensure that the benchmark loan approximates the 'comparable commercial loan which the firm could actually obtain on the market' specified in Article 14(b)." This approach, followed by the Panel, was consistent with the Appellate Body's approach to Article 14(d) in *US – Softwood Lumber IV*, indicating that when a proxy is used, the method for calculating the benefit should relate to or be connected with prevailing market conditions in the market of provision.[546] When this flexibility is exercised by the investigating authority, it

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540. *Id.* paras. 475–476.

541. *Id.* paras. 478–479.

542. *Id.* para. 482.

543. *Id.* para. 484.

544. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450; Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 10.119.

545. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 487.

546. *Id.* para. 488.

must assure that the benchmark is adjusted to approximate the "comparable commercial loan," and adequately and transparently explain the analysis.[547]

3) Rejection of Chinese Interest Rates as Benchmarks

Next, the Appellate Body considered whether the Panel properly applied this approach to the facts in the present case. China had faulted the Panel for failing to establish that the DOC's failure to rely on interest rates in China as the benchmark for loans by SOCBs was inconsistent with Article 14(b). In the three investigations, the DOC had relied on a study in the *Coated Free Sheet Paper* case,[548] because there was little new evidence regarding the Chinese government's role in the banking sector or any change in that role; nor did China suggest that any changes had occurred.[549] In its analysis, the Panel had drawn a distinction between a government's role as the setter and implementer of general monetary policy and its participation as a lender in the market in such a manner that the government rather than the market establishes lending rates. The latter role, in the Panel's view, could justify rejection of interest rates in a given market.[550]

China objected to this distinction, arguing that such an analysis meant that all interest rates would be distorted. Moreover, Articles 14(d) and 14(b) are different because, while governments do not typically establish prices for goods, they do establish benchmark interest rates. Also, according to China, neither the DOC nor the Panel demonstrated how certain factors such as China's regulatory limits on interest rates and government influence on SOCB lending decisions had any influence on interest rates.[551] The Appellate Body disagreed, supporting the Panel's distinction as well as its reliance on *US – Softwood Lumber IV*.[552] The Appellate Body noted that while "governments may establish or act to influence the 'discount rate' . . . [t]here is, however, a fundamental difference between the discount rate and the interest rates that banks charge to individual borrowers."[553] The former does not eliminate competition and thus distort commercial bank lending rates.[554] It also expressed approval of the Panel's determination that the DOC's reliance on a one-year-old study of the Chinese government's role in the banking sector was not inappropriate.[555]

The Appellate Body also rejected China's interpretation of *US – Softwood Lumber IV*, noting that in that case, the Appellate Body did not

547. *See id.* para. 489.

548. *See supra* note 457 and accompanying text.

549. *Id.* para. 492.

550. Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 10.126.

551. *See* Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, paras. 496–497 (quoting China's appellant's submission).

552. *Id.* paras. 498–499.

553. *Id.* para. 500.

554. *Id.*

555. *See id.* para. 502.

"establish a specific requirement that, to reject in-country prices, investigating authorities must show that government prices are artificially low."[556] Rather, the Appellate Body accepted that the DOC was entitled to establish that the various relevant factors—the government's predominant role as a lender, regulation of interest rates, and influence over SOCB lending decisions—taken together distorted the national commercial lending market sufficiently that a comparison of rates in the same market would not be meaningful for the purpose of Article 14(b).[557]

4) Proxy Benchmarks Used by the DOC

The Appellate Body noted that the "proxy was based on a regression analysis of inflation-adjusted interest rates in 33 lower-middle-income countries, on the basis of a 'broad inverse relationship' that the USDOC found between income levels and lending rates." This interest rate data was further adjusted to assure "comparability" in terms of political stability, government effectiveness, rules of law, and inflation; the DOC also excluded data from other NMEs and other countries where it judged the interest rates "anomalous."[558] China objected on grounds that the use of such a basket of foreign interest rates could not possibly be a "comparable commercial loan" under Article 14(b) and thus the Panel's acceptance of it without obtaining a "meaningful explanation" from the DOC violated the Panel's "objective assessment" obligations under the DSU, Article 11.[559]

China's views largely prevailed with the Appellate Body. The Appellate Body faulted the Panel for failing "to engage in a critical and searching review of whether the reasons put forth by the USDOC justified the proxy that it constructed, including in the light of other plausible alternatives."[560] Nor did it accept the Panel's contention that China had made no specific arguments as to the flaws in the DOC's methodology.[561] Rather, it faulted the Panel for simply accepting the DOC's determination and supporting evidence, and for failing to conduct "a sufficiently rigorous review of the USDOC's construction of its proxy benchmark."[562]

On the basis of these deficiencies, the Appellate Body reversed the Panel's findings on "objective assessment" grounds, but as usual declined to complete the analysis for lack of adequate undisputed facts in the record and Panel findings.[563]

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556. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 506.
557. *See id.* para. 508.
558. *Id.* para. 510.
559. *Id.* paras. 511–513.
560. *Id.* para. 523.
561. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 524.
562. *Id.* para. 526.
563. *Id.* paras. 527, 530, 537.

d. Double Counting of Anti-Dumping and CVDs

The Appellate Body began this aspect of its review by explaining the problem:

> "[D]ouble remedies" may arise when both countervailing duties and anti-dumping duties are imposed on the same imported products. The term "double remedies" does not, however, refer simply to the fact that both an anti-dumping and a countervailing duty are imposed on the same product. Rather, as explained below, "double remedies", also referred to as "double counting", refers to circumstances in which the simultaneous application of anti-dumping and countervailing duties on the same imported products results, at least to some extent, in the offsetting of the same subsidization twice. "Double remedies" are "likely" to occur in cases where an NME methodology is used to calculate the margin of dumping.[564]

The Appellate Body continued:

> [T]he dumping margin calculated under an NME methodology "reflects not only price discrimination by the investigated producer between the domestic and export markets ('dumping')", but also "economic distortions that affect the producer's costs of production", including specific subsidies to the investigated producer of the relevant product in respect of that product. An anti-dumping duty calculated based on an NME methodology may, therefore, "remedy" or "offset" a domestic subsidy, to the extent that such subsidy has contributed to a lowering of the export price. Put differently, the subsidization is "counted" within the overall dumping margin. When a countervailing duty is levied against the same imports, the same domestic subsidy is also "counted" in the calculation of the rate of subsidization and, therefore, the resulting countervailing duty offsets the same subsidy a second time. Accordingly, the concurrent imposition of an anti-dumping duty calculated based on an NME methodology, and a countervailing duty may result in a subsidy being offset more than once, that is, in a double remedy.[565]

564. *Id.* para. 541.

565. *Id.* para. 543 (quoting Panel Report, *US – AD/CVD (China)*, *supra* note 485, paras. 14.69–14.70).

The United States had effectively admitted that double remedies might result from this situation, but argued that "the existence of a double remedy depends on whether the subsidy leads to a reduction in the export price in any given instance, and contended that it cannot be presumed that domestic subsidies lower export prices pro rata, or one-for-one."[566] According to China, the Panel effectively decided that although Articles 19.3 and 19.4 of the SCM Agreement did not expressly prohibit offsetting the same domestic subsidies through the imposition of two different duties, the drafters did not intend to authorize such double counting. Rather, China asserted that the imposing Member was under an affirmative duty to prevent imposition of both countervailing duties and anti-dumping duties against the same subsidy on the same product.[567]

The principal question before the Appellate Body was the proper interpretation of SCM Agreement Article 19.3, which provides:

> When a countervailing duty is imposed in respect of any product, such countervailing duty shall be levied, *in the appropriate amounts in each case*, on a non-discriminatory basis on imports of such product from all sources found to be subsidized and causing injury, except as to imports from those sources which have renounced any subsidies in question or from which undertakings under the terms of this Agreement have been accepted. Any exporter whose exports are subject to a definitive countervailing duty but who was not actually investigated for reasons other than a refusal to cooperate, shall be entitled to an expedited review in order that the investigating authorities promptly establish an individual countervailing duty rate for that exporter.[568]

The Appellate Body emphasized two requirements: that the duty be in appropriate amounts and that it be non-discriminatory.[569] The two terms "inform" each other[570] and relate as well to Article 19.4, in that Article 19.4 "places a quantitative ceiling on the amount of a countervailing duty, which may not exceed the amount of the subsidization."[571]

However, Article 19.4 does not define the "universe" of "appropriateness." Rather, said the Appellate Body:

> [While] expressly leaving to the importing Member's investigating authorities the decision as to whether the amount

566. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 544.

567. *Id.* para. 545.

568. *Id.* para. 551 (emphasis added by the Appellate Body); SCM Agreement, *supra* note 245, art. 19.3.

569. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 552.

570. *Id.* para. 553.

571. *Id.* para. 554.

> of the countervailing duty to be imposed shall be the full amount of the subsidy or less, Article 19.2 nevertheless states that it is "desirable" that "the duty should be less than the total amount of the subsidy if such lesser duty would be adequate to remove the injury." Article 19.2 thus encourages such authorities to link the actual amount of the countervailing duty to the injury to be removed.[572]

And, under Article 19.2 of the SCM Agreement, investigating authorities are encouraged to assure that the amount of the countervailing duty be linked to the injury.[573]

In this analysis, context is also provided by the SCM Agreement, Article 10, titled "Application of Article VI of GATT 1994[*]":

> Members shall take all necessary steps to ensure that the imposition of a countervailing duty[**] on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement. Countervailing duties may only be imposed pursuant to investigations initiated and conducted in accordance with the provisions of this Agreement and the Agreement on Agriculture.[574]
>
> * [Original footnote 35] [W]ith regard to the effects of a particular subsidy in the domestic market of the importing Member, only one form of relief (either a countervailing duty, if the requirements of Part V are met, or a countermeasure under Articles 4 or 7) shall be available . . . .
>
> ** [Original footnote 36] The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise, as provided for in paragraph 3 of Article VI of GATT 1994.

The Appellate Body considers it important that this provision relates the SCM Agreement to Article VI of GATT, in that the first footnote confirms there can be only "one form of relief" under the system and that the second footnote defines a countervailing duty as a special duty to offset a subsidy.[575]

572. *Id.* para. 557 (footnotes omitted).
573. *Id.* para. 557.
574. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 559.
575. *Id.* para. 560.

Similarly, the Appellate Body finds Article 32.1 of the SCM Agreement significant in confirming the link between the Agreement and GATT 1994.[576] Article 32.1 provides in pertinent part:

> No specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement.[*]
>
> * [Original footnote 56] This paragraph is not intended to preclude action under other relevant provisions of GATT 1994, where appropriate.[577]

According to the Appellate Body, the provision and footnote "reaffirms" Members' rights to act under provisions of GATT 1994, provided that such actions are "appropriate."[578] Thus, other provisions of the SCM Agreement (Articles 10, 19.1, 19.2, 19.4, 21.1, and 32.1) provide context that is relevant to the interpretation of Article 19.3 because they identify "two situations in which the importing Member is prohibited from imposing two remedial measures as a response to the same subsidization."[579] Members seeking to impose remedies must choose between countermeasures under Parts II and III of the SCM Agreement (relating to actions before the DSB) and either price undertakings or countervailing duties. Also, the provisions confirm the "close link" between Part V of the SCM Agreement (countervailing duties) and Article VI of GATT 1994, including the relationship of the amount of countervailing duties to the injury caused to the domestic industry, as with parallel provisions of the Anti-Dumping Agreement.[580]

The Appellate Body next turned its analysis to what is probably the key legal provision for its inquiry, Article VI:5 of GATT 1994:

> No product of the territory of any contracting party imported into the territory of any other contracting party shall be subject to both anti-dumping and countervailing duties to compensate for the same situation of dumping or *export* subsidization.[581]

The Panel, noting that this provision applied explicitly to export subsidies, stated: "Members could not have intended to prohibit the imposition of double remedies

576. *Id.* para. 561.

577. SCM Agreement, *supra* note 245, art. 32.1; *see* Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 561.

578. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 562.

579. *Id.* para. 563.

580. *Id.*

581. *Id.* para. 565 (emphasis added).

in respect of domestic subsidies in Articles 19.3 or 19.4 of the SCM Agreement, which are, on their face, silent on the issue of double remedies."[582]

The Appellate Body was concerned with the Panel's "mechanistic, *au contrario* reasoning" and rejected it. Rather, the Appellate Body said that Article VI:5 prohibits the concurrent application of AD duties and CVD for the same situation and that there is a reason domestic subsidies are not expressly prohibited.[583] As the Appellate Body explained:

> [I]n principle, an export subsidy will result in a pro rata reduction in the export price of a product, but will not affect the price of domestic sales of that product. That is, the subsidy will lead to increased price discrimination and a higher margin of dumping. In such circumstances, the situation of subsidization and the situation of dumping are the "same situation," and the application of concurrent duties would amount to the application of "double remedies" to compensate for, or offset, that situation.[584]

However, with domestic subsidies, the situation is different:

> [D]omestic subsidies will, in principle, affect the prices at which a producer sells its goods in the domestic market and in export markets in the same way and to the same extent. Since any lowering of prices attributable to the subsidy will be reflected on both sides of the dumping margin calculation, the overall dumping margin will not be affected by the subsidization.[585]

In this situation of domestic subsidies, therefore, only the countervailing duty, not the AD duty, would offset the subsidies.[586] This analysis assumes that normal value, the usual method, is utilized for calculating the dumping margins based on the comparable price in the domestic market for the like product. But margins may be calculated based on exceptional methods, such as surrogate values, as permitted under Article VI:1 of GATT 1994,[587] and it is only in such

582. *Id.* para. 566 (quoting Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 14.118).

583. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 567.

584. *Id.* para. 568 (footnotes omitted).

585. *Id.*

586. *Id.*

587. *See* GATT B.I.S.D. § IV/58–76 (Annex A), notes 1, 2 to art. VI, para. 1; Notes and Supplementary Provisions, GATT B.I.S.D. § IR/61–74 (Annex H), notes 1, 2 to art. VI, para. 1 (1955); Notes and Supplementary Provisions, GATT B.I.S.D. § III/65–80 (Annex I), notes 1, 2 to art. VI, para. 1 (1958).

"exceptional" cases that there could be double counting between AD and CVD based on domestic subsidies.[588]

The Appellate Body noted that the "appropriate amounts" specified in Article 19.3 of the SCM Agreement "must not be based on a refusal to take account of the context offered both by Article VI of the GATT 1994 and by the provisions of the Anti-Dumping Agreement." Further, the Appellate Body was "not persuaded that it necessarily follows that these provisions are, as the Panel noted, 'oblivious to any potential concurrent imposition of anti-dumping duties.'"[589] The Appellate Body further observed that "Members have entered into cumulative obligations under the covered agreements and should thus be mindful of their actions under one agreement when taking action under another."[590]

Following this rationale, the "appropriate amounts" under Article 19.3 of the SCM Agreement cannot be properly determined without "due regard" to appropriate provisions of the Anti-Dumping Agreement because while "the purpose of each authorized remedy may be distinct . . . the form and effect of both remedies are the same." Further, both agreements place ceilings on the maximum duties to be imposed as respective remedies.[591] Therefore:

> Only if these provisions are read in wilful isolation from each other can it be maintained that the respective rules on the imposition and levying of duties are complied with when double remedies are imposed. In contrast, reading the two agreements together suggests that the imposition of double remedies would circumvent the standard of appropriateness that the two agreements separately establish for their respective remedies .... In other words . . . it should not be possible to circumvent the rules in each agreement by taking measures under both agreements to counteract the same subsidization.[592]

The Appellate Body then turned to the objective and purpose of the SCM Agreement but concluded that the Agreement did not provide "clear indications as to the intentions of the drafters . . . in respect of double remedies in case of domestic subsidization." At the same time:

> [W]e simply consider that the object and purpose of the *SCM Agreement* is not inconsistent with an approach that would accept that, in fixing the amount of countervailing duties that will be imposed, it is appropriate to take account of anti-

588. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 569.

589. *Id.* para. 570 (referring to Panel Report, *US – AD/CVD (China)*, *supra* note 485, paras. 14.112, 14.129).

590. *Id.*

591. *Id.* para. 571.

592. *Id.* para. 572.

> dumping duties that are being levied on the same products and that offset the same subsidization.[593]

Moreover, the Panel in this case improperly rejected China's assertion that the Panel's report in *EC – Salmon (Norway)*, interpreting Article 9.2 of the Anti-Dumping Agreement, was applicable. There, "the panel found that the appropriate amount of an anti-dumping duty 'must be an amount that results in offsetting or preventing dumping, when all other requirements for the imposition of anti-dumping duties have been fulfilled.'"[594] The Appellate Body found this interpretation of Article 9.2 consistent with its own interpretation of Article 19.3 of the SCM Agreement, that "an appropriate amount of countervailing duty should be an amount that results in offsetting subsidization, with due regard being had to the concurrent application of anti-dumping duties on the same product that offset the same subsidization." [595]

The Panel, in support of its conclusion that the Members had intended to allow double counting of AD and CVDs on imports from NMEs, had relied on Article 15 of the Tokyo Round Subsidies Code as context under Article 31 of the Vienna Convention on the Law of Treaties for interpreting the provisions of the SCM Agreement relating to double counting. However, the Appellate Body disagreed, deciding that the Code provisions, as part of a prior agreement, were at most a supplementary means of interpretation under Article 32 of the Vienna Convention.[596] The Appellate Body further noted that Article 15 of the Code prohibited all concurrent application of AD and CVDs, not just in the situation of double counting. Accordingly, the omission of such a provision in the SCM Agreement does not indicate that the Members intended to allow double counting in this narrower situation.[597]

Based on this analysis, the Appellate Body concluded that the Panel improperly interpreted Article 19.3 of the SCM Agreement:

> The amount of a countervailing duty cannot be "appropriate" in situations where that duty represents the full amount of the subsidy and where anti-dumping duties, calculated at least to some extent on the basis of the same subsidization, are imposed concurrently to remove the same injury to the domestic industry. Dumping margins calculated based on an NME methodology are, for the reasons explained above, likely to include some component that is attributable to subsidization.[598]

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593. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 574.

594. *Id.* para. 575 (referring to Panel Report, *European Communities – Anti-Dumping Measure on Farmed Salmon from Norway*, para. 7.705, WT/DS337/R (Nov. 16, 2007) (*adopted* Jan. 15, 2008)).

595. *Id.*

596. *Id.* paras. 577–579.

597. *See id.* para. 581.

598. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 582.

Rather, the imposition of double remedies through "the concurrent imposition of anti-dumping duties calculated on the basis of an NME methodology and countervailing duties, is inconsistent with Article 19.3."[599]

Given this conclusion, was it possible for the Appellate Body to complete the analysis (or decide such analysis was unnecessary) and, as China requested, find that the United States had engaged in double counting in the instant cases? Or should the Appellate Body have declined to complete the analysis because, as asserted by the United States, China failed to demonstrate, based on undisputed evidence, that double counting had occurred?[600] While the Panel accepted that double remedies would "likely" arise from concurrent application of AD and CVD with the use of NME methodology for the AD determination, the Panel considered that it did not need to examine "the extent to which the concurrent imposition of anti-dumping duties determined under the USDOC's NME methodology and of countervailing duties resulted in the imposition of 'double remedies' in the four investigations at issue."[601] The Panel also noted that the Department of Commerce had not alleged that it had taken the problem of double counting remedies into consideration.[602]

If double counting is prohibited, who has the burden of showing that it did not occur? The parties disagreed: "On appeal, China claims that it is 'the obligation of the investigating authority to *investigate* and make a determination as to whether it is offsetting the same subsidies twice,' whereas the United States argues that 'the burden to establish the existence of such an alleged double remedy would be on China.'"[603]

Not surprisingly, the Appellate Body reasoned that the burden is on the investigating authority. In *US – Certain EC Products*, the Appellate Body found that "under Article VI:3 of the GATT 1994, investigating authorities, before imposing countervailing duties, must ascertain the precise amount of a subsidy attributed to the imported products under investigation."[604] The Appellate Body found a parallel between Article VI:3 of GATT 1994 and the analogous obligation of the investigating authority under Articles 19.3 and 19.4 of the SCM Agreement "to determine and levy countervailing duties in amounts that are appropriate in each case and that do not exceed the amount of the subsidy found to exist."[605] Accordingly:

> In the same way, therefore, as an investigating authority is subject to an affirmative obligation to ascertain the precise amount of the subsidy, so too is it subject to an affirmative

599. *Id.* para. 583.

600. *Id.* paras. 593–594.

601. *Id.* para. 596 (quoting Panel Report, *US – AD/CVD (China)*, *supra* note 485, paras. 14.67, 14.76).

602. *Id.* para. 597; Panel Report, *US – AD/CVD (China)*, *supra* note 485, para. 14.105.

603. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 600.

604. Appellate Body Report, *US – Certain EC Products*, supra note 272, para. 139.

605. Appellate Body Report, *US – AD/CVD (China)*, *supra* note 450, para. 601.

> obligation to establish the appropriate amount of the duty under Article 19.3. This obligation encompasses a requirement to conduct a sufficiently diligent "investigation" into, and solicitation of, relevant facts, and to base its determination on positive evidence in the record.[606]

Because the DOC made no attempt to determine whether the same subsidies would be offset twice through the imposition of both AD and CVDs, the DOC failed to comply with its obligations to determine the "appropriate" amount of duties under Article 19.3 of the SCM Agreement.[607] Moreover, the violation of Article 19.3 was sufficient to constitute a violation of Articles 10 and 32.1 of the SCM Agreement: "China was not required to advance further arguments to establish a consequential violation of Articles 10 and 32.1."[608]

5. Commentary

a. More Work for the Investigating Authority in Demonstrating That SOEs and SOCBs Are "Public Bodies"

The principal impact of the Appellate Body's determination as it affects the demonstration that an SOE or SOCB is a "public body" under Article 1 of the SCM Agreement is to confirm that the burden is on the investigating authority to demonstrate that the entity is not only majority-owned by the government, but also exhibits other aspects of "government," such as furthering public policy objectives, social considerations, and industrial policies; failure to use normal commercial risk-management techniques in approving or denying loans or contracts; and approval and control of management by the government and/or the party, among other relevant considerations. The Department of Commerce, over the course of several investigations, including the four that are the subject of this appeal, had amassed sufficient data on China's ownership and control of SOCBs to satisfy the Appellate Body that Chinese SOCBs are "public bodies" under Article 1.1(a)(1) of the SCM Agreement. In contrast, the DOC did not amass sufficient factual information with regard to SOEs providing inputs (such as steel)

606. *Id.* para. 602.

607. *See id.* paras. 604–606.

608. *Id.* para. 610. The Panel, having declined to find a violation of Article 19.3, did not address China's allegation of violations of Articles 10 and 32.1. SCM Agreement Article 10 provides in pertinent part: "Members shall take all necessary steps to ensure that the imposition of a countervailing duty on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement." *See* SCM Agreement, *supra* note 245, art. 10. The parallel GATT article provides that "[n]o specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement." *See* GATT 1994, *supra* note 64, art. 32.1.

to the industries under investigation and as a result failed to sustain its burden of proof as set out by the Appellate Body in these proceedings.

In the future, as a general rule, the investigating authority will be required to collect much more information from the government, SOEs, SOCBs, and other sources in every CVD investigation in which it is alleged that "public bodies" are serving as the vehicles for actionable subsidies. This is particularly true with SOEs, where the characteristics of individual SOEs are likely to differ significantly with regard to the criteria, in contrast to SOCBs, which appear to share most of the same levels of government control.

These requirements will inevitably and probably unavoidably add to the cost and complexity of such investigations, particularly for the responding entities and their appointed counsel. The questionnaires sent to the government, SOEs, and SOCBs will be longer and more detailed, and on-site verifications are likely to be of longer duration and even more thorough. Should any such entities fail to respond completely and comprehensively, one can reasonably expect that such responses will be penalized with increased reliance on "facts available,"[609] although this approach is not likely to pass Appellate Body muster unless the DOC demonstrates that it made every reasonable effort to obtain information and that such requests were rebuffed or ignored. Petitioners will also likely attempt to provide more detailed information from any available sources as to the relationships between respondent governments and any relevant SOEs and SOCBs.

In actions before the Panel, moreover, it can be expected that the Panelists will request additional information from the responding Member (principally China and Vietnam) regarding the ownership of SOEs where the respondent is challenging its status as a public body. This may complicate the process and lead to frustration (and even adverse inferences by the Panel) if the responding Member is not perceived to be fully cooperating.[610]

One tactical challenge for petitioners and investigating authorities will be to decide whether to include alternative evidence in the administrative record to guard against a future Panel or Appellate Body decision determining that the authority has not met its burden of proving "public body" status for affected entities. Such evidence might demonstrate that even if one or more of the relevant SOEs or SOCBs were considered not to be public bodies, said entities were entrusted or directed by the government "to carry out one or more of the type of functions . . . which would normally be vested in the government and the practice,

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609. SCM Agreement, *supra* note 245, art. 12.7 ("In cases in which any interested Member or interested party refuses access to, or otherwise does not provide, necessary information within a reasonable period or significantly impedes the investigation, preliminary and final determinations, affirmative or negative, may be made on the basis of the facts available.").

610. *See, e.g.*, Panel Report, *Turkey – Measures Affecting the Importation of Rice*, paras. 2.50–2.57, 7.90–7.106, WT/DS334/R (Sept. 21, 2007) (*adopted* Oct. 22, 2007) (where Turkey refused to provide certain information the Panel requested, resulting in obvious Panel annoyance and a possible impact on the results).

in no real sense, differs from practices normally followed by governments."[611] Presumably, that determination would follow the requirements set out by the Appellate Body in earlier proceedings, such as *US – DRAMS*,[612] where the Appellate Body confirmed that certain bank lending in Korea met the "entrust or directs" requirements.

b. The Appellate Body Reaches the Obvious Conclusion on Double Counting

Few observers could have been surprised by the Appellate Body's determination that the Department of Commerce's assessment of simultaneous anti-dumping and countervailing duties on the same imports was considered inconsistent with U.S. obligations under Article VI:5 of GATT and Articles 19.3 and 19.4 of the SCM Agreement, particularly where the DOC made no effort to deal with the probable double counting. Whether the DOC can devise a method that sufficiently takes this problem into account remains to be seen. To many, this dilemma seems an inevitable result of treating China as a non-market economy for anti-dumping purposes while effectively treating China as a market economy in important respects for countervailing duty purposes.

The critical problem, as noted earlier in quotations from the Appellate Body Report, is that an anti-dumping duty determination based on surrogate country values rather than home market values means that any domestic subsidization is necessarily included within the overall dumping margin to the extent that the subsidy results in a decrease in the export price. If CVDs are applied to the same imports based on same domestic subsidy, that subsidy is counted in the calculation of the rate of subsidization as well, and the resulting countervailing duty offsets the same subsidy a second time. The problem for the DOC and any other investigating authority is accurately correcting for the double counting. This issue is not limited to the Appellate Body; the U.S. Court of International Trade reached the same conclusion, although the appeal was decided on different grounds, as discussed immediately below.

c. U.S. Court of Appeals for Federal Circuit Voids the DOC's NME CVD Practice on Other Grounds

Because of the alleged double counting, several Chinese respondents sought relief from the U.S. Court of International Trade (CIT). Initially, the CIT remanded the DOC's action of parallel AD/CVD duties against China back to the

611. SCM Agreement, *supra* note 245, art. 1.1(a)(iv).

612. Appellate Body Report, *United States – Countervailing Duty Investigation on Dynamic Random Access Memory Semiconductors (DRAMS) from Korea*, paras. 120–26 WT/DS296/AB/R (June 27, 2005) (*adopted* July 20, 2005); *see* Raj Bhala & David A. Gantz, *WTO Case Review 2005*, 23 ARIZ. J. INT'L & COMP. L. 107, 173 (2006).

DOC.[613] The court reasoned that, unlike the situation in which the dumping duties in parallel AD and CVD actions in a market economy are calculated based on normal value and export price, in NME actions, the export price is not being compared with the price of the good in the domestic market, but rather, in a surrogate country market that is presumably subsidy-free.[614] Without adjustment, the court reasoned, such a situation could result in double counting.[615] CIT Judge Jane Restani criticized the DOC for failing to develop the necessary procedures for analyzing such requests from individual enterprises, which the DOC conceded was the situation.[616]

Judge Restani determined that the DOC's failure to address plaintiff GPX International's request for market-oriented economy (MOE) status "because it had no policies, procedures, or standards for evaluating MOE status was arbitrary and capricious and unsupported by substantial evidence."[617] The court, mindful as well of the conceptual inconsistency, held that "[i]f Commerce now seeks to impose CVD remedies on the products of NME countries as well [as AD duties], Commerce must apply methodologies that make such parallel remedies reasonable, including methodologies that will make it unlikely that double counting will occur."[618] In the final CIT decision after remand, the DOC was effectively ordered not to impose CVDs on NMEs without a change in methodology, confirming what Judge Restani opined in the initial decision.[619]

The Court of Appeals for the Federal Circuit affirmed, but on different grounds, leaving Judge Restani's holding on the double-counting issue intact. The Court of Appeals essentially ignored Judge Restani's reasoning, observing:

> [W]hen amending and reenacting countervailing duty law in 1988 and 1994, Congress legislatively ratified earlier consistent administrative and judicial interpretations that government payments cannot be characterized as "subsidies" in a non-market economy context, and thus that countervailing duty law does not apply to NME countries.[620]

Ultimately, the Court of Appeals concluded:

> We thus find that in amending and reenacting the trade laws in 1988 and 1994, Congress adopted the position that

613. GPX Int'l Tire Corp. v. United States, 645 F. Supp. 2d 1231, 1251 (Ct. Int'l Trade 2009).

614. *See id.* at 1245.

615. *See id.* at 1234–35.

616. *See id.* at 1243.

617. *Id.* at 1246.

618. *GPX Int'l Tire*, 645 F. Supp. 2d at 1243.

619. GPX Int'l Tire Corp. v. United States (GPX III), No. 08-00285, 2010 WL 3835022, at *1 (Ct. Int'l Trade Oct. 1, 2010).

620. GPX Int'l Tire Corp. v. United States, 666 F.3d 732, 734 (Fed. Cir. 2011).

> countervailing duty law does not apply to NME countries. Although Commerce has wide discretion in administering countervailing duty and anti-dumping law, it cannot exercise this discretion contrary to congressional intent. We affirm the holding of the Trade Court that countervailing duties cannot be applied to goods from NME countries.[621]

This decision, based on the administrative law doctrine of "legislative ratification," effectively meant that the DOC could not apply U.S. CVD laws to NMEs (with or without double counting) unless the U.S. Supreme Court granted certiorari and reversed, or Congress modified the laws to explicitly permit the DOC to apply them to NMEs. A legislative "fix" was quickly enacted in March 2012.[622] As noted earlier, many in Congress had been urging the DOC to apply the CVD laws to China before the change in policy in 2006. Moreover, given the broad concern in Congress and elsewhere about China's allegedly unfair trade practices and WTO violations, including but not limited to currency manipulation,[623] legislators of both parties were highly receptive to a change in the law that would overrule the GPX decision, be WTO compliant, and at the same time facilitate bringing unfair trade actions against China.

The new law explicitly authorizes the DOC, retroactively to November 20, 2006, to continue applying the CVD law to China, effectively reversing the Court of Appeals decision. Through such retroactivity, the legislation is designed to permit some twenty-four existing CVD orders and six pending investigations against China to continue.[624] The law also permits the Commerce Department to adjust anti-dumping duties assessed on goods from an NME where CVDs are applied to the same goods.[625] It explicitly provides that where the DOC "can reasonably estimate the extent to which the countervailable subsidy . . . has increased the weighted average dumping margin for the class or kind of merchandise . . . [it may] reduce the anti-dumping duty by the amount of the increase in the weighted average dumping margin estimated by the administering authority . . . ."[626]

Whether the law, if applied to pending CVD and AD orders, will pass constitutional muster remains to be seen. The Court of Appeals, in May 2012,

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621. *Id.* at 745.

622. *See* Brevetti, *supra* note 466 (reporting the signing of H.R. 4105 by President Obama on March 13, 2012).

623. *See International Finance: House Democrats Fail in Bid to Bring Up China Currency Measure*, 28 INT'L TRADE REP. (BNA) 1935 (Dec. 1, 2011) (reporting that the House refused consideration of a currency reform bill favored by the Democrats, which had passed the Senate in October).

624. S. 2153, 112th Cong., § 1(a) (2012).

625. *See* Brevetti, *supra* note 466.

626. S. 2153, § 2(a); *see* Press Release, Baucus, Thune Applaud Senate Passage of Bill to Defend American Jobs, Fight Unfair Chinese Subsidies (Mar. 5, 2012), *available at* http://insidetrade.com/iwpfile.html?file=mar2012%2Fwto2012_0468.pdf.

remanded a challenge to the CIT and directed the CIT to consider the law's constitutionality.[627]

d. Implementation by the United States

The United States and China agreed in July 2011 that the "reasonable period of time"[628] for implementation of the Panel and Appellate Body reports would be eleven months, or by February 25, 2012. This period was later extended to April 25, 2012, by agreement of the parties.[629] Despite the deadline, resolution of the dispute remains pending; the United States advised the WTO in July 2012 of the internal administrative steps that the U.S. government was taking to implement the reports, including the enactment of legislation that clarifies the application of U.S. CVD laws to NMEs.[630]

E. Trade Remedies: Special Safeguards Against China

1. Citation

Appellate Body Report, *United States – Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China*, WT/DS399/AB/R (September 5, 2011) (*adopted* October 5, 2011) (complaint by China).

2. Background

Since 1947, the GATT has provided for safeguards under Article XIX and, since 1995, under the Agreement on Safeguards.[631] However, not every safeguard relief measure arises under GATT Article XIX. That much is evident from the Uruguay Round agreements, such as the Agreement on Agriculture, which (in Article 5) establishes a special safeguard for farm products, and from the now-elapsed Agreement on Textiles and Clothing, which (in Article 6) created

627. GPX Int'l Tire Corp. v. United States, 678 F.3d 1308, 1313 (Fed. Cir. 2012).

628. DSU, *supra* note 3, art. 21.3 ("If it is impracticable to comply immediately with the recommendations and rulings, the Member concerned shall have a reasonable period of time in which to do so.").

629. Modification of the Agreement Under Article 21.3(b) of the DSU, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, WT/DS379/13 (Jan. 19, 2012).

630. Status Report by the United States, *United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, WT/DS379/12/Add.6 (July 13, 2012).

631. Agreement on Safeguards, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 154 (1994).

a transitional safeguard mechanism. It also is evident from the tortuous and ultimately unsuccessful Doha Round negotiations over a special safeguard mechanism. Yet another example of escape clause-like relief that is not related to Article XIX is a product-specific safeguard, which famously was negotiated in the context of China's Accession Protocol. That Accession became effective on December 11, 2001, and the special remedy associated with China is, logically enough, sometimes called the "China-specific safeguard," or more generally, a "country-specific safeguard."[632]

This case concerns a safeguard measure imposed by the United States under Section 421 of the United States Trade Act of 1974, as amended, upon tires ("tyres" in British orthography) for passenger and light truck vehicles from China.[633] Section 421 is legislation that implements the product-specific safeguard set out in the Protocol. The product-specific safeguard in the Protocol was temporary, scheduled to expire at the end of 2013. Thus, Section 421 also will sunset at that time.

The tires investigation was not the first Section 421 action brought against China. In four of six previous instances, the International Trade Commission (ITC or USITC) adjudicated such cases and recommended relief, but President George W. Bush declined to provide such relief.[634] In the fifth Section 421 case, President Barack Obama agreed to follow the ITC recommendation in favor of relief. In so doing, he catalyzed a dispute that ultimately landed before the WTO Appellate Body. His invocation of Section 421 in 2009 was the first, and perhaps only, use of the product-specific safeguard against China in the world.[635]

The facts of the Appellate Body case, *United States – Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China* are as follows.[636] On April 20, 2009, the ITC received an initial complaint regarding the subject merchandise, tires, from the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial, and Service Workers International Union.[637] The resulting safeguard measure against the tires entered into force on September 26, 2009.[638]

The period of investigation (POI) was from 2004 to 2008. The ITC divided the relevant tire market into two separate markets: the replacement market and the original equipment manufacturer (OEM) market. The replacement market "consists of customers buying tyres to use as replacement tyres for cars *already* on

632. *See* China's Accession Protocol, *supra* note 470, pt. 1, para. 16.

633. *See* Panel Report, *US – Tyres*, *supra* note 9, para. 2.1.

634. *See* Amy Tsui, *Trade Policy: Progress Still Possible in U.S.-China Trade; Trade Enforcement Center Adds to Tensions*, 29 INT'L TRADE REP. (BNA) 618 (Apr. 19, 2012).

635. *See id.*

636. *See* Appellate Body Report, *US – Tyres*, supra note 9.

637 *See* Panel Report, *US – Tyres*, *supra* note 9, para. 2.2.

638. *See id.*

the road" and "accounts for about 80% of the total US market."[639] The ITC further divided the replacement market into three tiers. Those tiers were based on brand and price.[640] Tier one consisted of premium brands. Tier two was made up of "secondary, associate, or foreign producer brands."[641] Tier three "includes private label, mass market, lesser-known brands, and non-branded tyres."[642] As for the OEM market, it "consists of tyres produced for sale to manufacturers of *new* passenger vehicle and light trucks" and "represents about 20% of the total US market."[643] The ITC did not further subdivide the OEM market into distinct categories.

Following an affirmative determination and recommendation for relief from the ITC, President Obama approved a final safeguard remedy. That remedy consisted of an additional tariff rate applied to subject merchandise for three years. The additional tariff rate for the first year was 35% ad valorem.[644] The tariff rate fell to 30% in the second year and dropped again to 25% in the third year.[645]

3. Appellate Issue One and Holdings

Before the Panel, China lost on every allegation it raised. Unfortunately for China, it also lost every issue it raised on appeal. China appealed two broad Panel decisions.

First, China claimed that the Panel erred in determining that the ITC properly found the subject merchandise was "increasing rapidly" within the meaning of Paragraph 16:4 of the Accession Protocol.[646] Second (as discussed in Part II.E.4.a. of this Case Review), China argued that the Panel erred in holding that the ITC properly found the subject merchandise to be "a significant cause" of material injury to the American domestic tire industry within the meaning of the Protocol.[647]

639. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 203 n.448 (emphasis added).

640. *See id.*

641. *Id.*

642. *Id.*

643. *Id.* para. 203 n.450.

644. *See* Panel Report, *US – Tyres*, *supra* note 9, para. 2.2.

645. *Id.*

646. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 115(a).

647. *See id.* para. 115(b).

a. Standard for Imports "Increasing Rapidly"?

The first issue before the Appellate Body was whether "the Panel erred in finding that the USITC properly determined that subject imports were 'increasing rapidly' within the meaning of Paragraph 16:4 of China's Accession Protocol."[648]

China and the United States offered conflicting definitions of "increasing rapidly." Therefore, the Appellate Body had to opine on the relevant legal standard before it could address the Chinese contention that the Panel erred in its assessment of "increasing rapidly."[649]

Paragraphs 16:1 and 16:4 of the Accession Protocol were relevant to determining the standard for "increasing rapidly." Paragraph 16:1 states:

> In cases where products of Chinese origin are being imported into the territory of any WTO Member in *such increased quantities or under such conditions as to cause or threaten to cause market disruption to the domestic producers of like or directly competitive products*, the WTO Member so affected may request consultations with China with a view to seeking a mutually satisfactory solution, including whether the affected WTO Member should pursue application of a measure under the Agreement on Safeguards. Any such request shall be notified immediately to the Committee on Safeguards.[650]

Manifestly, this language tracks, but is not verbatim with, that of GATT Article XIX. Paragraph 16:4 of the Protocol says:

> Market disruption shall exist whenever imports of an article, like or directly competitive with an article produced by the domestic industry, are *increasing rapidly*, either absolutely or relatively, so as to be a significant cause of material injury, or threat of material injury to the domestic industry. In determining if market disruption exists, the affected WTO Member shall consider objective factors, including the volume of imports, the effect of imports on prices for like or directly competitive articles, and the effect of such imports on the domestic industry producing like or directly competitive products.[651]

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648. *Id.* para. 126.
649. *See id.*
650. China's Accession Protocol, *supra* note 470, pt. 1, para. 16(1) (emphasis added).
651. *Id.* pt. 1, para. 16(4) (emphasis added).

China argued that the standard in the Protocol is higher for import increases than the analogous standards in safeguard provisions in other GATT-WTO texts.[652] The United States disagreed.

Beginning with a textual interpretation, China contended the word "'increasing' requires investigating authorities to focus on the most recent past."[653] China also said the adverb "'rapidly' implies a focus on the rates of increase in imports."[654] China fixed on the present tense form of the phrase "increasing rapidly." China claimed the use of the present tense distinguished the Protocol from other WTO agreements, which use the past tense.[655]

Next, China recalled the 2000 *Argentina – Footwear* case, where the Appellate Body commented on the "extraordinary" nature of safeguards under the WTO Agreement on Safeguards.[656] According to China, the Protocol shares this same "extraordinary" nature with that Agreement because the Protocol similarly establishes disciplines on "fair trade."[657] But, said China, the Protocol is even more trade-distorting than the Agreement on Safeguards; that is, a product-specific safeguard disfigures the import and export patterns to a greater degree than traditional GATT Article XIX escape clause relief.[658] Moreover, China argued that the Protocol "allows [for] the derogation . . . [from] the most-favoured nation (MFN) principle, because it provides for the application of trade-restrictive measures exclusively against China."[659] Thus, China said, "this 'extra-extraordinary' nature of measures under the *Protocol* must be taken into account" when defining what the "increasing rapidly" standard means.[660]

The United States offered a successful rebuttal. It explained that an investigating or administering authority (such as the ITC) may exercise discretion when establishing a POI and that the rate of increase in imports of subject merchandise is irrelevant. An investigating authority may "select any period, provided that it allows for an assessment of import increases during a 'recent period.'"[661] The Americans also argued that the rate of increase in imports does not matter because the adverb "'rapidly' . . . does not embody a 'comparative or relative concept.'"[662] As for textual and contextual comparisons between the product-specific safeguard in the Protocol and GATT-WTO safeguards, the United States dismissed them.[663] According to the United States, there are too

652. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 128.
653. *Id.* para. 127.
654. *Id.*
655. *See id.*
656. *Id.* para. 128 (quoting Appellate Body Report, *Argentina – Safeguard Measures on Imports of Footwear*, paras. 94–95, WT/DS121/AB/R (Dec. 14, 2000) (*adopted* Jan. 12, 2001) [hereinafter Appellate Body Report, *Argentina – Footwear*]).
657. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 128.
658. *See id.*
659. *Id.*
660. *Id.*
661. *Id.* para. 129.
662. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 129.
663. *See id.*

many differences between the Protocol and the other agreements to warrant the kind of comparison the Chinese attempted.[664]

Finally, the United States disputed the Chinese claim that the Protocol embodies a higher import-increase standard than GATT or other WTO agreements.[665] The Chinese read too much into the expression "extraordinary remedy" as used by the Appellate Body in the *Argentina – Footwear* case. Instead, the United States asserted:

> [T]he Appellate Body's conclusion that a safeguard measure is an "extraordinary remedy" stems from the express reference to "emergency actions" and "unforeseen developments" in the text of Article XIX of the GATT 1994, and neither of these terms are present in the text of Section 16 of the Protocol.[666]

To buttress their point, the Americans observed that the injury determination standard is lower in the Protocol than the WTO Agreement on Safeguards.[667] That legal fact further undermined the Chinese argument for a heightened standard under the Protocol.[668]

Following the 1969 Vienna Convention on the Law of Treaties, the Appellate Body examined the ordinary meaning and context of the phrases "increasing rapidly" and "absolutely or relatively" in Paragraph 16:4 of the Protocol and the phrases "are being imported" and "in such increased quantities" in Paragraph 16:1.[669] The Appellate Body examined, as it customarily does, the *Oxford English Dictionary*, along with the overall purpose of Paragraph 16.[670] To a limited extent, the Appellate Body also relied on its own precedent. Regarding the phrase "are being imported," the Appellate Body pointed to similar language in the *Argentina – Footwear* case. In that case, the Appellate Body determined the analogous phrase "is being imported" implied the increase was "sudden and recent."[671] The Appellate Body then extended that meaning to the phrase "are being imported" in the Protocol, finding:

> In sum, imports from China will be "increasing rapidly" under Paragraph 16.4 of the Protocol when they are *increasing at great speed or swiftly, either in relative or absolute terms*. Such import increases must be occurring over a *short and recent period of time*, and must be of a *sufficient absolute or relative*

664. *Id.*
665. *See id.* para. 130.
666. *Id.*
667. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 130.
668. *Id.*
669. *See id.* paras. 134–139.
670. *See id.* paras. 135, 137.
671. *Id.* para. 137 (quoting Appellate Body Report, *Argentina – Footwear*, *supra* note 656, para. 130).

> *magnitude so as to be a significant cause of material injury to the domestic industry*.[672]

The language highlighted above is how the Appellate Body defined whether imports are "increasing rapidly." In effect, it created a three-part test: great speed or swiftness, short and recent period, and sufficiency to be a significant cause of material injury.

b. Applying the "Increasing Rapidly" Standard

Did the ITC fail to prove the subject merchandise was "increasing rapidly"?[673] China said "yes," offering three arguments based on the fact that "a decline in the *rate* of increase in subject imports in the last year of the . . . period of investigation indicated that subject imports were not 'increasing rapidly' within the meaning of Paragraph 16.4."[674]

First, China claimed that the ITC should have focused more on the most recent part of the POI and less on earlier parts of that period.[675] Second, China urged that ITC was required to "focus . . . on the *rates* of increase in subject imports."[676] Third, China contended that the ITC was required to compare the rates of increase in subject imports from the most recent year to earlier years during the POI.[677] The Appellate Body examined and rejected each individual argument separately.

c. Argument About Most Recent Period

Concerning its first argument, China asserted that the Panel "erred in its interpretation of Paragraph 16:4 of the Protocol" and "erred in its application of the 'increasing rapidly' standard of Paragraph 16:4."[678] Regarding the misinterpretation, China claimed the use of the present tense "increasing," as opposed to the past tense "increased," requires the ITC to focus on the most recent year in the POI.[679]

China accused the Panel of improperly relying on the Agreement on Safeguards in its contextual interpretation. Regarding the misapplication, China claimed that "neither the USITC nor the Panel adequately explained why import increases over the full five-year period of investigation were relevant to a

672. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 140 (emphasis added).
673. *See id.* para. 141.
674. *Id.*
675. *See id.* para. 142.
676. *Id.* para. 154.
677. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 163.
678. *Id.* paras. 142–143.
679. *Id.* para. 142.

determination that imports were 'increasing rapidly' or should be accorded equal weight to the most recent import trends."[680]

The United States contended that investigating authorities have discretion to establish the POI, as long as it shows imports increased during a "recent period." The United States also asserted that the ITC "expressly reasoned that the two largest 'year-to-year increases' with respect to the ratio of the 'subject imports to U.S. production' and 'market share of the Chinese imports' occurred 'at the end of the period in 2007 and 2008.'"[681]

China lost the argument. The Appellate Body dismissed the Chinese claim that the present tense continuous "are increasing" requires investigators to "focus exclusively on import increases that occurred during the *most* recent past."[682] Relying partly on *Argentina – Footwear*, the Appellate Body said that although the POI must be recent enough to "provide a reasonable indication of current trends in imports," the analysis does not need to be "limited to import data relating to the very end of the period of investigation."[683] The Appellate Body also said that investigators need to compare the earlier and later periods within the POI to determine whether subject merchandise is "being imported . . . in such increased quantities" as Paragraph 16.1 of the Protocol requires.[684]

d. Argument About Rate of Increase in Subject Tires

Second, China claimed that "the Panel erred in its interpretation of Paragraph 16.4 of the Protocol in finding that the USITC was not required to focus its analysis on the *rates* of increase in subject imports."[685]

China argued that "'rapidly' is a relative concept, which conveys the idea that something is increasing more quickly than something else."[686] The United States responded that the Panel correctly found this adverb to mean "swiftly" or "quickly," as opposed to "more swiftly" or "more quickly."[687]

China also claimed that "the Panel erred in its application of Paragraph 16:4 when it upheld the USITC's 'inadequate' assessment of the *rates* of increase in subject imports."[688]

The Panel accepted the finding of the ITC that imports increased rapidly. China was unsatisfied with this finding because the rate of increase declined in the

680. *Id.* para. 143.
681. *Id.* para. 145.
682. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 146.
683. *Id.* para. 147 (citing Appellate Body Report, *Argentina – Footwear*, *supra* note 656, para. 130). *See also id.* para. 148 (refuting the Chinese claim that investigating authorities must "focus exclusively on the most recent period").
684. *Id.* para. 148.
685. *Id.* para. 154.
686. *Id.*
687. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 156.
688. *Id.* para. 155.

last year of the POI.[689] The United States responded that the ITC "did examine the rates of increase in subject imports in the final years of the period of investigation" and that it "emphasized that the 'two largest year to year increases' in these metrics occurred in 2007 and 2008."[690] The Appellate Body agreed with the Panel:

> [A] decline in the *rates* of increase in imports towards the end of the period of investigation does not detract from the USITC's conclusion that imports from China were "increasing rapidly", particularly when import increases at the end of the period of investigation remained significant both in relative and in absolute terms.[691]

This statement reflects long-standing safeguards jurisprudence that it is appropriate to examine rates in increase of subject merchandise in absolute terms and/or terms relative to production of the like domestic product. The fact that the rate of increase in either absolute or relative terms decelerates does not automatically detract from the force of the argument for imposing a trade remedy.

e. Argument About Comparison of Rates of Increase in Subject Tires

Third, China contended that investigating authorities such as the ITC must compare the rates of increase in subject imports from the most recent period to earlier periods during the POI.[692] Surely the phrase "increasing rapidly" suggests "imports must be increasing more rapidly than some other benchmark."[693] Furthermore, China argued that the ITC did not sufficiently explain why imports were found to be "'increasing rapidly' when the rate of increase in subject imports in 2008 was lower than the rates of increase in the previous years."[694] According to China, the lower ending rate does not indicate a "rapid" increase, as the Protocol requires.[695] The United States responded again that "'increasing rapidly' does not require an 'accelerating rate of increase' over the period of investigation."[696] The United States emphasized that the subject import volumes were reasonably determined to be increasing rapidly, not only in absolute terms, but also in relative terms.[697]

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689. *Id.*
690. *Id.* para. 157.
691. *Id.* para. 162.
692. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 163.
693. *Id.*
694. *Id.* para. 164.
695. *Id.*
696. *Id.* para. 165.
697. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 166.

The Appellate Body completely dismissed the Chinese allegations.[698] The ITC demonstrated sufficiently that the quantity of subject imports rose in the 2006-to-2007 and 2007-to-2008 periods within the POI and that the market share of subject merchandise increased in every part of the POI.[699]

Thus, after hearing all three separate arguments by China, the Appellate Body upheld the finding by the Panel that the ITC properly assessed "whether imports from China met the specific threshold under Paragraph 16.4 of China's Accession Protocol of 'increasing rapidly.'"[700] The bottom line is that an investigating authority has considerable discretion to examine trends in importation of subject merchandise within a POI; i.e., it is not confined to rendering an affirmative determination about increasing imports only where data show steady or accelerating rates. Put differently, the authority can draw inferences by comparing and contrasting different portions within a POI, including the starting and ending portions.

4. Appellate Issue Two and Holdings

a. Standard for "Significant Cause"?

The second issue on appeal was whether the ITC properly found that "rapidly increasing imports from China were 'a significant cause' of material injury to the domestic industry under Paragraph 16.4 of China's Accession Protocol."[701] Again, the Appellate Body began by addressing the legal standard of causation before examining the Chinese arguments.[702]

Conceptually, China made the same argument on this issue as on the first one; namely, that its Protocol sets a higher standard for imposition of a trade remedy than the analogous GATT-WTO trade remedy agreements. That is, China said the Protocol contains an enhanced standard of causation. Why? Because the Protocol, unlike other WTO texts, modifies "cause" with the adjective "significant."[703] And, as before, China argued the purpose of the Protocol reinforces the heightened standard because of the "'extra'-extraordinary nature" of the Protocol.[704]

The United States responded that the ordinary standard in trade remedy litigation under GATT-WTO texts, as interpreted by the Appellate Body, is "genuine and substantial" causation. The adjective "significant" does not increase the typical standard. Furthermore, the purpose of the Protocol does not support a heightened standard. The United States contrasted the Protocol with the title and

698. *See id.* paras. 167–168.
699. *See id.* para. 168.
700. *Id.* para. 170.
701. *Id.* para. 171.
702. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 172.
703. *See id.* para. 173.
704. *See id.*

language of GATT Article XIX: "measures under the Protocol are not 'emergency actions' resulting from 'unforeseen developments.'"[705] To the contrary, the Protocol explicitly sets out a lower injury threshold than does GATT.[706] The key inference the United States drew from comparing the Protocol and GATT was not to draw too strong an inference at all; there were important distinctions in their language and purposes.

The Appellate Body looked at the ordinary meaning of and the context surrounding the term "significant cause." The Appellate Body relied on the *Oxford English Dictionary* and precedent to determine the ordinary meaning of the words "significant" and "cause." The word "cause," according to the 2001 *US – Wheat Gluten* case, "denot[es] a relationship between, at least, two elements, whereby the first element has, in some way, 'brought about,' 'produced' or 'induced' the existence of the second element."[707]

After examining the ordinary meaning and context of "significant cause," the Appellate Body determined that "significant":

> [D]escribes the causal relationship or nexus that must be found to exist between rapidly increasing imports and material injury to the domestic industry, which must be such that rapidly increasing imports make an "*important*" *or* "*notable*" contribution in bringing about material injury to the domestic injury. Such assessment must be carried out on the basis of the objective factors listed in the second sentence of Paragraph 16.4 . . . .[708]

Here again, the Appellate Body consumed paragraphs and pages to define a key term ("significant") in a manner both obvious and nearly tautological ("important" or "notable"). For the reader well-versed in Appellate Body reports, the pattern was familiar: practicing law and adjudicating cases using synonyms from a treasured dictionary, rather than providing deep insights or brilliant tests.

In any event, the Appellate Body dismissed the claim by China that the use of "significant" creates a higher causation standard than other WTO accords. The Appellate Body also noted that the purpose of Paragraph 16 of the Protocol was "to afford temporary relief to domestic industries that are exposed to market disruption as a result of a rapid increase in Chinese imports of like or directly

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705. *Id.* para. 174.

706. *See id.*

707. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 176 (quoting Appellate Body Report, *United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities*, para. 67, WT/DS166/AB/R (Dec. 22, 2000) (*adopted* Jan. 19, 2001) (in turn quoting THE NEW SHORTER OXFORD ENGLISH DICTIONARY 1958 (4th ed. 1993))).

708. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 180 (emphasis added).

competitive products, subject to the conditions and requirements provided therein."[709]

Accordingly, the Appellate Body found that the purpose of the Protocol did not bolster the Chinese argument.[710] The Appellate Body also noted that the Protocol has a lower injury threshold than the other WTO agreements, as argued by the United States.[711] The Appellate Body concluded:

> Paragraph 16.4 of the Protocol sets forth a distinct causation standard whereby rapidly increasing imports must be "a *significant* cause" of material injury to the domestic industry. This causation standard requires that rapidly increasing imports from China make an *important contribution* in bringing about material injury to the domestic industry.[712]

The Appellate Body also noted that a finding of causation must be determined by "objective criteria," according to the second sentence of Paragraph 16:4.[713] The Appellate Body then examined the standard in light of the individual arguments made by China regarding causation. Regarding its first argument concerning conditions of competition, China claimed that the ITC was required to look at the "*degree of competitive* overlap between imported and domestic products, and . . . identify a coincidence both in the 'year-by-year changes' and in the 'degree of magnitude' between subject imports and injury factors."[714] The United States disagreed and re-emphasized that the Protocol does not contain a heightened causation standard.[715] The United States argued that there is no "specific methodology" to determine causation, nor is there a requirement of "correspondence between the magnitude of changes in subject imports and the magnitude of changes in the performance indicators of the domestic industry."[716]

The Appellate Body determined that Paragraph 16:4 allows for some discretion by investigating authorities to determine a specific methodology to determine causation. However, it stressed that the methodology must "establish[] that rapidly increasing imports are 'a significant cause' of material injury to the domestic industry, and consider[] the objective factors listed in the second sentence of Paragraph 16.4."[717]

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709 *Id.* para. 184.
710. *See id.*
711. *See id.* para. 183.
712. *Id.* para. 185 (emphasis added).
713. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 185.
714. *Id.* para. 186.
715. *See id.* para. 187.
716. *Id.*
717. *Id.* para. 191.

Succinctly put, methodologies will be reviewed on a case-by-case basis, which, the Appellate Body noted, is in accordance with its 2011 *Airbus* decision.[718]

The Appellate Body recognized conditions of competition and "correlation between movements in imports and injury factors are merely 'analytical tools.'"[719] As such, neither is "dispositive" to the determination of causation.[720] Regarding the correlation between movements in imports and injury factors, the Appellate Body again looked to the 2000 *Argentina – Footwear* case.[721] There, the Appellate Body found that even if there is no correlation between those two variables, subject merchandise still could be the cause of injury, if there is "a *very* compelling analysis of why causation still is present."[722]

China also offered a non-attribution claim; namely, there is "an inherent requirement to consider other possible causes of injury" when determining causation.[723] The heightened standard in the Protocol means investigating authorities must look at the separate effects of subject imports and other possible causes of injury.[724] The United States asserted that China mistakenly relied on the 2001 *Lamb Meat* and *Hot-Rolled Steel* cases to justify its argument.[725] The United States asserted that those cases relied on specific language in the WTO Anti-Dumping and Safeguards Agreements that is inapplicable to the language in the Protocol.[726]

The United States did not gainsay the need for a non-attribution analysis. An investigating authority must consider the effects of other possible causal factors in relation to injury. But that the authority has discretion in determining how to assess their effects.[727]

The Appellate Body looked at its 2008 compliance-decision *Cotton* case, as had the Panel and the United States.[728] Following its *Cotton* decision, the Appellate Body said that even in the absence of explicit language, there must be some analysis of the "injurious effects" of factors other than the subject

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718. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 191; *see* Appellate Body Report, *EC – Airbus*, *supra* note 8, para. 1376.

719. *Id.* para. 192.

720. *Id.*

721. *Id.* para. 193; *see* Appellate Body Report, *Argentina – Footwear*, *supra* note 656, para. 144.

722. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 194 (quoting Appellate Body Report, *Argentina – Footwear*, *supra* note 656, para. 144).

723. *Id.* para. 196 (quoting China's appellant's submission).

724. *See id.*

725. *See id.* para. 198; *see also* Appellate Body Report, *United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia*, WT/DS177/AB/R, WT/DS178/AB/R (May 1, 2001) (*adopted* May 16, 2001); Appellate Body Report, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/AB/R (July 24, 2001) (*adopted* Aug. 23, 2001).

726. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 198.

727. *See id.*

728. *See* Appellate Body Report, *US – Upland Cotton* compliance, *supra* note 393.

merchandise to show the subject merchandise meets the causation standard under Paragraph 16:4 of the Protocol.[729] Whether the effects of other factors are properly analyzed is a case-by-case determination.[730]

What is interesting about this Appellate Body statement is its context. The statement would be considered commonplace for trade remedies based directly on provisions in GATT or a Uruguay Round text. But here, the Appellate Body is saying that non-attribution analyses are relevant to remedies specially created in terms of accession. In sum, then, the teaching on causation from the *US – Tyres* case is modest: "significant cause" is defined in a somewhat circular way to mean "important" or "notable" contribution in leading to the material injury of a domestic industry, and to confirm this contribution, a non-attribution analysis is necessary.

b. Applying the Causation Standard

Next, the Appellate Body turned to application of the causation standard. China made three distinct arguments as to why the ITC improperly determined that the subject merchandise was "a 'significant cause' of material injury to the domestic industry."[731]

First, China asserted that the conditions of competition in the domestic tire market showed "'attenuated' competition between subject imports and domestic tyres."[732] According to China, the ITC failed to properly analyze the conditions of competition in the replacement market, the original equipment manufacturer market, and the overall market (the replacement and OEM markets combined). Second, China argued that the ITC improperly relied on "an 'overall coincidence' between import increases and declines in injury factors" when determining causation.[733] Finally, China argued that the ITC did not "address adequately the individual and cumulative effects of other causal factors" in its causation determination.[734] The Appellate Body addressed each argument separately and, in the end, upheld the Panel's holding.

729. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 201.

730. *See id.*

731. *Id.* para. 171.

732. *Id.*

733. *Id.*

734. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 171. China also claimed that the Panel violated Article 11 of the DSU. The Appellate Body said that although the Panel "could have provided more reasoning to support its findings," the Panel did not violate Article 11 of the DSU. *Id*. para. 337.

c. Argument About Conditions of Competition

The first argument concerned conditions of competition in the American tire market. China contested the Panel finding that there was significant competition between subject merchandise and domestic tires in the replacement market. China made distinct arguments concerning the analysis of conditions of competition in the replacement market, the OEM market, and in the overall market. The Appellate Body dealt with each one separately, starting with the replacement market.

Its discussion, like the Chinese arguments, was legalistic, even tedious. But the thrust of the Chinese contention was this: a nuanced understanding of the three types of tire markets and of distinctions within the replacement market showed that subject merchandise did not compete directly, at least not to any major degree, with American tires. Consequently, Chinese imports could not possibly have been the "significant cause" of the woes of the American tire producers.

To be sure, the ITC did break up the tire replacement market into three tiers (premium brands in tier one, and cheaper brands in tiers two and three). China criticized the lack of "bright-line distinctions" between those tiers, especially between the second and third tiers.[735] China asserted that the Panel failed to focus on "how the existence of those segments affected the USITC's conclusion that competition between imports from China and domestic tyres in the U.S. replacement market was not attenuated."[736]

China claimed that the ITC did not fully analyze evidence suggesting that the majority of domestic tire production occurred in tier one, where the domestic industry faced extremely limited competition from Chinese tire producers. Instead, subject merchandise tended to be more prevalent in the second and third tiers. According to China, conditions of competition, even in tiers two and three, were not a reasonable basis on which to find that its tires were "a significant cause" of material injury to the domestic industry.[737]

The United States responded that "significant quantities" of domestic and Chinese tires competed in tiers two and three in the last POI, which sufficiently showed competition between the subject merchandise and domestic tires.[738] The United States asserted that "unclear demarcations between the tiers of the U.S. replacement market did not support China's argument that imports in one tier could not impact volumes and prices in another tier of the market."[739]

The Appellate Body commented that the lack of completely distinct tiers "suggests a greater degree of competitive overlap across these tiers than otherwise would have existed had such tiers been clearly delineated."[740] The Appellate

735. *See id.* para. 204.
736. *Id.* para. 207.
737. *Id.* para. 203.
738. *See id.* para. 205.
739. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 205.
740. *Id.* para. 208.

Body noted that the Panel wrongly relied on statements by dissenting ITC commissioners and one Chinese producer in finding that there were no distinct dividing lines between the tiers of the replacement market.[741]

However, the Panel also properly relied on several other reasons, such as sufficient market share data in the second and third tiers, to justify its overall conclusion that the ITC properly determined significant competition existed between the subject merchandise and domestic tires in the American replacement market.[742] Therefore, despite the error, the Appellate Body upheld the Panel finding.

China also was concerned about conditions of competition within the OEM market. China said American producers focused more on the OEM market than the replacement market.[743] China asserted that the Panel "should have assessed whether competition in [the OEM] market was significant," as opposed to focusing on trends in imports of Chinese tires.[744] According to China, competition from Chinese tire producers in the OEM market was, in fact, insignificant.[745] China pointed out that the OEM market share for the subject merchandise was no more than 5% during the POI.[746] The lack of competition in both the OEM and tier one replacement market pointed to a "'highly attenuated' degree of competition between Chinese imports and domestic tyres in the U.S. market."[747] Regrettably, said China, neither the Panel nor the ITC gave a reasonable explanation about causation in light of this dearth of competition.[748]

The United States provided a successful rebuttal: the presence of Chinese tires in the OEM market was growing, and, in turn, there was significant competition in the entire market.[749] According to the United States, the OEM market share for subject imports grew during the POI, while the OEM market share for domestic tires decreased.[750] The United States also noted that "a volume of 2.3 million tyres from China, representing a 5% market share in 2008, could not be considered 'negligible.'"[751]

The Panel had also rejected China's assertion that the volume of subject merchandise was "negligible."[752] The Panel determined that the volume of domestic tire shipments decreased by 46% over the 2004-to-2008 POI.[753]

741. *See id.* para. 211.
742. *See id.* para. 215.
743. *See id.* para. 203.
744. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 216.
745. *See id.* para. 203.
746. *See id.* para. 216.
747. *Id.* para. 203.
748. *See id.*
749. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 217.
750. *See id.*
751. *Id.*
752. *See id.* para. 218.
753. *See id.*

Conversely, the volume of subject tire shipments increased by a whopping 1,785% during the same period.[754]

The Appellate Body upheld the Panel's finding yet criticized the Panel for relying primarily on an "end-point-to-end-point comparison of relative volumes and market share" in finding an increasing degree of competition between the domestic tires and subject merchandise in the OEM market.[755] It did so because of its own precedents. In several previous cases, such as *Argentina – Footwear*, *EC – Airbus*, and *Steel Safeguards*, the Appellate Body "expressed reservations" over such end-point-to-end-point comparisons.[756] Ultimately, the Appellate Body recognized that the Panel, while relying too heavily on the end-point comparison, did do a minimal amount more by looking beyond the OEM market to the overall market.[757] The Appellate Body commented that it would have preferred a more detailed assessment of the ITC analysis of the OEM market. But it agreed that the OEM market is less important than the replacement market for Chinese and American producers.

Finally, China argued that "the Panel failed to grasp the significance of the combined effect of attenuated competition in the OEM and replacement markets for its review of the USITC's assessment of the conditions of competition in the overall US market."[758] China cast doubt on the finding of the Panel and the ITC concerning causation, given that "approximately 60% of US production went into Tier One of the replacement market and the OEM market, where Chinese imports held only a 2%–3% combined market share."[759]

The United Stated responded that the Panel and the ITC properly found:

> [T]here was "significant competition" between Chinese and domestic tyres in tiers 2 and 3 of the U.S. replacement market, that Chinese imports in different segments could impact prices and volumes of domestic tyres in other segments because there were "no clear dividing lines" between the tiers of the replacement market, and that subject imports were taking a "growing though smaller" share of the OEM market.[760]

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754. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 218.

755. *See id.* para. 219.

756. *See id.* para. 220; *see also* Appellate Body Report, *Argentina – Footwear*, *supra* note 656; Appellate Body Report, *EC – Airbus*, *supra* note 8; Appellate Body Report, *United States – Definitive Safeguard Measures on Imports of Certain Steel Products*, WT/DS248/AB/R, WT/DS249/AB/R, WT/DS251/AB/R, WT/DS252/AB/R, WT/DS253/AB/R, WT/DS254/AB/R, WT/DS258/AB/R, WT/DS259/AB/R (Nov. 10, 2003) (*adopted* Dec. 10, 2003).

757. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 219.

758. *Id.* para. 221.

759. *Id.*

760. *Id.* para. 222 (footnotes omitted).

For reasons redolent of those it offered with respect to the replacement and OEM markets, the Appellate Body rejected the Chinese contentions with respect to the overall market. The Appellate Body said the overall effect of the "significant presence" of subject merchandise in tiers two and three of the replacement market, and the increasing presence of subject merchandise in tier one of the replacement market and the OEM market, was enough to uphold the Panel finding. The Appellate Body said the degree of competition in the replacement market "was sufficient to establish that competition in the *overall* U.S. market was significant."[761] Thus, the Appellate Body confirmed that the "USITC did not err in its assessment of the conditions of competition in the overall U.S. market."[762]

d. Argument About the Correlation Between Increases in the Subject Merchandise and Injury

China also argued that the ITC improperly relied on a "coincidence" in a correlation between increases in subject merchandise and material injury to establish causation.[763] The Panel should have required "a more specific degree of correlation," said China; instead, the Panel neglected to explain fully an apparent "'disconnect in the trends between 2007 and 2008."[764] China also argued that the Panel failed to "take into account the effects of 'attenuated competition' on underselling, and failed to address adequately the fact that non-subject imports also undersold domestic tyres."[765]

China asserted that the ratio of the cost of goods sold to sales (COGS/sales) in 2007 showed that domestic tire producers did not actually "suffer[] a 'cost price squeeze' over the period of investigation."[766]

The United States responded that the Protocol "did not require a strict correlation in the degrees of changes in subject imports and injury factors."[767] The United States claimed a number of "injury indicators"—such as production, net sales, and hours worked—dropped each year during the POI. Other variables, including operating margins, productivity, and operating income, fell during three of the four years during the POI. According to the United States, despite improvement of some factors in 2007, the Panel correctly found an overall correlation.[768] The United States also rejected China's position that "an improvement in the COGS/sales ratio in 2007 suggested an absence of correlation."[769]

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761. *Id.* para. 224.
762. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 226.
763. *Id.* para. 227.
764. *Id.* para. 228.
765. *Id.* para. 229.
766. *Id.* para. 242.
767. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 230.
768. *Id.*
769. *Id.* para. 231.

China lost the argument. First, the Appellate Body looked at the alleged "trend disconnect" between 2007 and 2008.[770] The Chinese argument was based on an implicit assumption that the Protocol mandated a "stricter degree of correlation" than other WTO agreements.[771] That was a false assumption, said the Appellate Body. Recalling *Argentina – Footwear*, the Appellate Body emphasized: "the analysis of correlation focuses on 'the *relationship* between *movements* in imports (volume and market share) and the *movements* in injury factors.'"[772] The Appellate Body also intoned that this case stood for another, related proposition: while correlation can suggest "a causal link," it is not by itself dispositive.[773]

Indeed, the Appellate Body agreed with the Panel that determining a correlation between increases in the subject merchandise and worsening injury factors is "not an exact science."[774] According to the Appellate Body, a correlation analysis should attempt to show "a *temporal* coincidence between an upward trend in *subject imports* and a downward trend in the performance indicators of the domestic industry . . . ."[775] There is no requirement that these trends move in "strict simultaneity."[776]

That is, given that increases in subject merchandise imports may be affected differently, even uniquely, by different injury factors, it does not make sense to require strict correlation between those imports and the injury factors.[777] China insisted on a lock-step march, with subject merchandise imports rising and injury factors worsening. A flexible, case-by-case approach is preferable—though of course it cannot be too malleable, either—and a "trend disconnect" is not fatal to the claim of the complainant in a product-specific safeguard action. Consequently, the Appellate Body also was unconvinced by the data and correlations China offered to support its argument.

The Appellate Body also looked at the correlation between import increases, domestic prices, and profitability, specifically the improvement in the COGS/sales ratio in 2007. The Appellate Body agreed with the Panel that "the COGS/sales ratio in 2007 does not *per se* undermine the finding of the ITC that subject imports negatively affected domestic prices."[778] The Appellate Body said that because there is not a strict correlation requirement, the increased ratio in three out of the four years during the POI is sufficient to support the determination by the Panel that the ITC assessment was reasonable.[779]

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770. *Id.* para. 235.

771. *Id.* para. 236.

772. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 237 (quoting Appellate Body Report, *Argentina – Footwear*, *supra* note 656, para. 144).

773. *Id.* para. 237.

774. *Id.* para. 238 (quoting Panel Report, *US – Tyres*, *supra* note 9, para. 7.229).

775. *Id.* para. 239.

776. *Id.*

777. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 238.

778. *Id.* para. 245.

779. *Id.*

Certainly, the Appellate Body noted, one injury factor of many is not necessarily determinative of overall injury. What matters is that the assessment by an investigating authority is reasonable and follows the causation standard. (As explained in Part II.E.4.b., a "significant cause" is an "important" or "notable" contribution to the material injury of a domestic injury.)[780] In the end, the Appellate Body upheld the Panel finding that "the USITC's reliance on an overall coincidence between an upward movement in subject imports and a downward movement in injury factors reasonably supports" the determination of causation by the ITC.[781]

e. Argument About Other Causes of Injury

As for the non-attribution analysis that forms an indispensable part of an inquiry into causation, China claimed that the ITC did not properly address causes of injury other than those attributed to the subject merchandise. The Panel relied on the 2005 Appellate Body Report in *Cotton* to determine that a non-attribution analysis was required, even though there is no express mandate for one in the Protocol.[782] The Appellate Body agreed with the Panel. That agreement was tantamount to an impressive bit of interstitial lawmaking: the Appellate Body was applying a causation standard established for other trade remedies to the product-specific safeguard in the Protocol.

According to the Appellate Body, "some form of non-attribution analysis is *inherent* in the establishment of a causal link between rapidly increasing imports from China and material injury to the domestic injury."[783] The Appellate Body declared:

> This determination [of causation] can only be made if an investigating authority properly ensures that effects of other known causes are not such as to suggest that subject imports are in fact only a "remote" or "minimal" cause, rather than a "significant" cause of material injury to the domestic industry.[784]

The Appellate Body noted that whether an assessment of other factors has been properly conducted is established on a case-by-case basis.[785] Therefore, some

780. *Id.* para. 246.

781. *See id.* para. 249.

782. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 251; Appellate Body Report *US – Upland Cotton*, *supra* note 234.

783. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 252.

784. *Id.*

785. *See id.* China also disputed a particular statement by the Panel regarding causation. China claimed, based on the statement, that the Panel used an "'all or nothing' approach to the assessment" of other causal factors. *Id.* para. 254. The Appellate Body

cases necessarily require a comprehensive analysis, while other cases call for a less thorough one.

China attributed the injury suffered by the American tire industry to three factors other than Chinese imports.[786] The first factor was the American industry's business strategy. China argued that the domestic industry voluntarily shifted production from lower value tires manufactured in foreign countries to higher value tires manufactured in the United States.[787] According to China, this production shift created "a 'supply gap' in the U.S. market that was filled by imports from both China and other sources."[788]

However, the ITC determined that this shift was involuntary and was a reaction to the increase in subject merchandise from China.[789] The ITC based its finding on relevant news articles and evidence related to plant closings by large American tire manufacturers.[790] The Appellate Body examined the record and said the Panel analysis was adequate. The Panel did not err "in its review of the USITC's analysis of the U.S. domestic industry's business strategy and the reasons for the three U.S. plant closures."[791]

China claimed that the second causal factor the Panel failed to "evaluate seriously" was a decline in American consumer demand for tires.[792] China presented data showing a decrease in demand throughout the POI, followed by a sharper decline in 2008 due to economic recession.[793] The United States countered that the demand fluctuated, but even during periods of diminished demand, the market share of Chinese producers increased.[794] Conversely, the market share of American producers decreased at a rate consistent with the decline in demand.[795] Therefore, decrease in domestic demand did not explain the injury to the domestic industry.[796]

The Appellate Body examined the record and determined that the Panel "carefully examined the correlation between trends in subject imports and changes in demand over the full period of investigation."[797] The Appellate Body also emphasized that the "bulk" of the decrease in demand occurred during the recession in 2008, which both the Panel and the ITC took care to analyze

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rejected this argument, saying the wording by the Panel was unfortunate; nonetheless, the Panel showed that it had an appropriate understanding of the causal standard. *Id.* at paras. 256–258.

786. *See id.* para. 259.
787. *See id.* para. 262.
788. Appellate Body Report, *US – Tyres*, *supra* note 9 para. 262.
789. *Id.* para. 263.
790. *Id.*
791. *Id.* para. 284.
792. *See id.* paras. 259, 285.
793. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, para. 285.
794. *See id.* para. 287.
795. *See id.* para. 301.
796. *See id.* para. 256.
797. *See id.* para. 290.

separately.[798] The Appellate Body determined that the Panel was right to uphold the ITC determination that "subject imports had injurious effects independent of any injury caused by changes in demand."[799]

China asserted that the third causal factor was non-subject imports from foreign countries other than China.[800] China claimed that non-subject imports had greater market share than subject merchandise, yet their competitive effects were not considered by the ITC.[801] China also claimed that non-subject imports were lower priced than American tires.[802] Notably, China did not say whether non-subject tires were priced lower than subject tires. The Panel noticed that the market share of non-subject tires declined during the POI, as did the market share of American tires.[803] It drew the obvious inference: the decline in market share was associated with the rise in market share of Chinese tires. As for underpricing by non-subject merchandise, the Panel said those goods had a higher unit value than did subject merchandise. The Panel did not explain this point well, but it seems to have thought that the per-tire value of non-subject tires was greater than that of Chinese tires; therefore, a comparison of tire prices was simplistic.

Overall, then, the Panel said that the Chinese points about the market share and pricing of non-subject merchandise were unpersuasive. In truth, their impact on injuring the American tire industry was much less than the effects of subject merchandise on that industry. The Appellate Body agreed and determined that the Panel did not err in finding that the ITC assessment was reasonable.

Finally, China claimed the Panel erred in finding that China "failed to establish that in the context of the present case, the USITC should have provided a cumulative assessment of the effects of the other causes of injury."[804] The appellate argument was largely the same as what China put to the Panel.[805] Moreover, this argument was founded on an improper understanding of the causation standard set forth in Paragraph 16:4 of the Protocol.[806] The Appellate Body determined that the Panel's analysis was sufficient; i.e., it upheld the Panel finding that the ITC properly attributed injury to the subject merchandise from China.[807] In turn, the Appellate Body agreed with the Panel that the ITC "properly established that rapidly increasing imports from China were 'a

798. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 294 (citing Panel Report, *US – Tyres*, *supra* note 9, para. 7.339).

799. *Id.* para. 298 (quoting Panel Report, *US – Tyres*, *supra* note 9, para. 7.333).

800. *See id.* para. 259.

801. *See id.* para. 299.

802. *See id.*

803. *See* Appellate Body Report, *US – Tyres*, *supra* note 9, paras. 301–302 (citing Panel Report, *US – Tyres*, *supra* note 9, para. 7.353).

804. *Id.* para. 309 (quoting Panel Report, *US – Tyres*, *supra* note 9, para. 7.377).

805. *Id.* para. 311.

806. *See id.* para. 318.

807. *Id.* para. 319.

significant cause' of material injury to the U.S. domestic industry within the meaning of Paragraph 16:4 of the Protocol."[808]

With this conclusion, the second of the two steps was complete. Imports of subject merchandise had increased rapidly during the POI (step one), and that increase caused injury to the domestic producer of a like or directly competitive product (step two).

5. Commentary

a. Extending Existing Trade Remedy Jurisprudence to Protocol-Based Remedies

In the *US – Tyres* case, the Appellate Body held that:

- "Increasing rapidly" means that subject merchandise rises in an absolute or relative sense, with great speed or swiftness, in a short and recent period, and with sufficiency to be a significant cause of material injury; and
- "Significant cause" means an "important" or "notable" contribution leading to the material injury of the allegedly afflicted domestic industry, as confirmed by a non-attribution analysis that covers a range of objective factors to ensure causation is not wrongly attributed to subject merchandise.

In reaching these holdings, the Appellate Body interpreted language peculiar to China's Accession Protocol. It might well have been tempted to issue idiosyncratic rulings; i.e., definitions of key terms specific to that Protocol. To some extent, it did. The holdings do spring from the product-specific safeguard. But the larger message of the *US – Tyres* case is the extent to which the Appellate Body tried to square its holdings with those in trade-remedy disputes arising out of standard GATT-WTO texts. In effect, the Appellate Body appears to extend much of its jurisprudence from those texts to the China-Specific Safeguard.

That is clear from its repeated citation to itself in the *Argentina – Footwear* and *Cotton* cases, and its rejection of Chinese arguments that the language of the Protocol mandates a higher standard for imposition of the Safeguard than the standard in those other texts. It might be remarked that de facto stare decisis lurks in the *Tyres* case, as the Appellate Body (and Panel) rationalized its opinions not just on provisions specific to the Accession Protocol, but also on precedent regarding other WTO agreements. Doing so further harmonizes key legal terminology and concepts throughout all the WTO agreements. Put colloquially, the Appellate Body seemed to say that while the

808. Appellate Body Report, *US – Tyres*, *supra* note 9, para. 115(b).

China-Specific Safeguard is a distinct remedy, in practice it really is not that different from other safeguards.

Why might the Appellate Body essentially equalize, or nearly so, a safeguard carved out in an accession protocol with existing comparable remedies? After all, is the Appellate Body not one of the last powerful bastions of free trade? Should it not make it harder, not easier, to impose protectionist measures?

One answer is that it is consciously trying to spin the proverbial seamless web of the law. Why have multiple disjointed remedies with radically different legal triggers where a broadly consistent set will suffice? Another answer is that the Appellate Body was fearful of emasculating a trade remedy the United States and other major trading powers deliberately created for use against China. Consider the counter-factual: the Appellate Body agrees with the Chinese arguments that the product-specific safeguard has far higher standards for imposition than other GATT-WTO remedies. That finding would infuriate China's trading partners, who negotiated an extra, if nearly redundant, remedy for both political and economic cover with domestic constituents. Such a finding would vitiate the political and economic purposes of the remedy because the higher trigger standards would make it nearly impossible to use.

b. Safeguards, Politics, and Consolation for China

After a few important wins in WTO litigation, China must have felt it suffered a great blow in the *Tyres* case. Not only did China lose every claim before the Panel, but it also lost every argument in each of its appeals. China staked much in the case on its underlying political perception about the product-specific safeguard; namely, that it was a remedy targeting China.

That perception was accurate. The remedy was indeed a country-specific one. But it was a remedy to which China had agreed in 2001. It had no choice. When China negotiated for WTO accession, it did so amid a worldwide climate of fear that its manufacturing might lead to import surges in many WTO Member countries. The Members felt that GATT Article XIX was not enough to protect them against Chinese competition, so to the "belt" of this Article they added the "suspenders" of the country-specific remedy.

China could take consolation from two facts. First, the United States imposed the contested safeguards in this case pursuant to Section 421 of its Trade Act. Section 421 expires on December 11, 2013, twelve years after China joined the WTO. Second, it was the only such safeguard action the United States has pursued to date, over almost eleven years.