

**UNITED STATES – IMPOSITION OF COUNTERVAILING DUTIES ON  
CERTAIN HOT-ROLLED LEAD AND BISMUTH CARBON STEEL  
PRODUCTS ORIGINATING IN THE UNITED KINGDOM**

**REPORT OF THE PANEL**

The report of the Panel on United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom is being circulated to all Members, pursuant to the DSU. The report is being circulated as an unrestricted document from 23 December 1999 pursuant to the Procedures for the Circulation and Derestriction of WTO Documents (WT/L/160/Rev.1). Members are reminded that in accordance with the DSU only parties to the dispute may appeal a panel report. An appeal shall be limited to issues of law covered in the Panel report and legal interpretations developed by the Panel. There shall be no *ex parte* communications with the Panel or Appellate Body concerning matters under consideration by the Panel or Appellate Body.

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TABLE OF CONTENTS

	<u>Page</u>
<b>I. INTRODUCTION .....</b>	<b>1</b>
<b>II. FACTUAL ASPECTS .....</b>	<b>1</b>
<b>III. ARGUMENTS OF THE PARTIES .....</b>	<b>3</b>
<b>IV. THIRD PARTIES .....</b>	<b>3</b>
A. BRAZIL .....	3
B. MEXICO.....	17
<b>V. INTERIM REVIEW .....</b>	<b>22</b>
A. COMMENTS BY THE EUROPEAN COMMUNITIES .....	22
B. COMMENTS BY THE UNITED STATES .....	22
<b>VI. FINDINGS .....</b>	<b>23</b>
A. INTRODUCTION .....	23
B. PRELIMINARY ISSUES .....	23
C. WERE THE COUNTERVAILING DUTIES IMPOSED AS A RESULT OF THE 1995, 1996 AND 1997 ADMINISTRATIVE REVIEWS CONSISTENT WITH ARTICLES 10 AND 19.4 OF THE SCM AGREEMENT? .....	29
<b>VII. CONCLUSION .....</b>	<b>47</b>
<b>VIII. RECOMMENDATION .....</b>	<b>47</b>
<b>ATTACHMENT 1: EUROPEAN COMMUNITIES' SUBMISSIONS .....</b>	<b>48</b>
<b>1.1 FIRST SUBMISSION OF THE EUROPEAN COMMUNITIES .....</b>	<b>48</b>
<b>1.2 ORAL STATEMENT AND CONCLUDING STATEMENT         OF THE EUROPEAN COMMUNITIES AT THE FIRST MEETING         WITH THE PANEL .....</b>	<b>80</b>
<b>1.3 RESPONSES OF THE EUROPEAN COMMUNITIES         TO WRITTEN QUESTIONS FROM THE PANEL – FIRST MEETING .....</b>	<b>93</b>
<b>1.4 RESPONSES OF THE EUROPEAN COMMUNITIES         TO WRITTEN QUESTIONS FROM THE UNITED STATES – FIRST MEETING...</b>	<b>96</b>
<b>1.5 SECOND SUBMISSION OF THE EUROPEAN COMMUNITIES .....</b>	<b>109</b>
<b>1.6 ORAL STATEMENT OF THE EUROPEAN COMMUNITIES         – SECOND MEETING .....</b>	<b>135</b>
<b>1.7 RESPONSES OF THE EUROPEAN COMMUNITIES         TO WRITTEN QUESTIONS FROM THE PANEL – SECOND MEETING .....</b>	<b>148</b>

	<u>Page</u>
<b>IV. ATTACHMENT 2: UNITED STATES' SUBMISSIONS.....</b>	<b>162</b>
<b>2.1 FIRST WRITTEN SUBMISSION OF THE UNITED STATES .....</b>	<b>162</b>
<b>2.2 ORAL STATEMENT OF THE UNITED STATES         AT THE FIRST MEETING OF THE PANEL.....</b>	<b>208</b>
<b>2.3 RESPONSES OF THE UNITED STATES TO QUESTIONS         FROM THE PANEL – FIRST MEETING.....</b>	<b>220</b>
<b>2.4 RESPONSES OF THE UNITED STATES TO QUESTIONS         FROM THE EUROPEAN COMMUNITIES – FIRST MEETING .....</b>	<b>233</b>
<b>2.5 SECOND SUBMISSION OF THE UNITED STATES .....</b>	<b>241</b>
<b>2.6 ORAL STATEMENT OF THE UNITED STATES – SECOND MEETING.....</b>	<b>254</b>
<b>2.7 FINAL STATEMENT OF THE UNITED STATES – SECOND MEETING.....</b>	<b>268</b>
<b>2.8 RESPONSES OF THE UNITED STATES TO QUESTIONS         FROM THE PANEL - SECOND MEETING .....</b>	<b>270</b>

## I. INTRODUCTION

1.1 On 12 June 1998, the European Communities requested consultations with the United States pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), Article XXII:1 of the General Agreement on Tariffs and Trade 1994 (GATT 1994) and Article 30 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement) with respect to the imposition of countervailing duties by the United States on certain hot-rolled lead and bismuth carbon steel products (lead bars) originating in the United Kingdom in the context of three successive annual reviews (WTO document WT/DS138/1). The European Communities and the United States held consultations on 29 July 1998, but failed to reach a mutually satisfactory solution.

1.2 On 14 January 1999, pursuant to Articles 4 and 6 of the DSU, Article XXIII of the GATT 1994 and Article 30 of the SCM Agreement, the European Communities requested the establishment of a panel with respect to the imposition of countervailing duties by the United States on certain hot-rolled lead and bismuth carbon steel products originating in the United Kingdom in the context of three successive annual reviews (WTO documents WT/DS138/3 and WT/DS138/3/Corr.1).

1.3 At its meeting on 17 February 1999, the Dispute Settlement Body (DSB) established a panel pursuant to the above request. At that meeting, the parties to the dispute agreed that the Panel should have standard terms of reference. The terms of reference were:

"To examine, in light of the relevant provisions of the covered agreements cited by the European Communities in documents WT/DS138/3 and WT/DS138/3/Corr.1, the matter referred to the DSB by the European Communities in that document and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements".

1.4 On 16 March 1999, the Panel was constituted as follows:

Chairman:	Mr. Ole Lundby
Members:	Mr. Paul O'Connor
	Mr. Arie Reich

1.5 Brazil and Mexico reserved their rights as third parties to the dispute.

1.6 The Panel met with the parties on 15-16 June 1999 and 14-15 July 1999. It met with the third parties on 16 June 1999.

1.7 The Panel submitted its interim report to the parties on 6 October 1999. On 20 October 1999, both parties submitted written requests for the Panel to review precise aspects of the interim report. On 8 November 1999, each party filed comments on the written request submitted by the other party. Neither party requested a further meeting with the Panel. The Panel submitted its final report to the parties on 22 November 1999.

## II. FACTUAL ASPECTS

2.1 This dispute concerns the imposition of countervailing duties by the United States on certain hot rolled lead and bismuth carbon steel products originating in the United Kingdom in the context of three successive annual reviews.

2.2 On 8 May 1992, a countervailing duty investigation was initiated by the United States against imports of hot rolled lead and bismuth carbon steel from, *inter-alia*, the United Kingdom. The period of investigation was calendar year 1991. On 27 January 1993, the United States Department of

Commerce (USDOC) issued a final determination establishing a subsidy rate of 12.69 per cent on imports from United Engineering Steels Limited (UES).<sup>1</sup> On 22 March 1993, following an affirmative injury determination by the United States International Trade Commission (USITC), the USDOC published a countervailing duty order at the above rate on imports from UES.

2.3 During the period of investigation, UES was a joint-venture equally owned by British Steel Public Limited Company (British Steel plc) and Guest, Keen and Nettlefolds (GKN), both of which were privately-owned companies. The alleged subsidies countervailed were not provided to either co-owner of UES but to state-owned British Steel Corporation (BSC). BSC established UES in 1986 in association with GKN. British Steel plc was related to BSC in the sense that the former assumed the property, rights and liabilities of the latter in September 1988. The British government privatized British Steel plc in December 1988 through a sale of shares. Both parties agree that the privatization of British Steel plc was "at arm's length, for fair market value and consistent with commercial considerations".

2.4 On 21 March 1995, UES became a wholly-owned affiliate of British Steel plc as this company bought out GKN's interests. UES was subsequently renamed British Steel Engineering Steels (BSES).

2.5 The alleged subsidies countervailed relate principally to equity infusions granted by the British Government to BSC during fiscal years 1977/78 – 1985/86. The USDOC classified such alleged subsidies as non-recurrent and thus spread them out over 18 years, deemed to be the useful life of productive assets in the steel industry. The USDOC found that the alleged subsidies in question "passed through" from BSC to UES first, and then more recently to BSES.

2.6 Following the original imposition of CVDs in March 1993, the DOC has undertaken six annual reviews to set the duty rate on imports of the subject product. The first review is not being challenged as it was initiated on 15 April 1994, prior to the entry into force of the SCM Agreement. The fifth review, initiated on 24 April 1998, is not being challenged either as it was completed (11 August 1999) after the request for establishment of the Panel (WTO documents WT/DS138/3 and WT/DS138/3/Corr.1). Similarly, the sixth review, initiated on 30 April 1999, is not subject to challenge given that it was opened after the request for establishment of the Panel. Therefore, the subject of this Panel are the outcomes of the second, third and fourth reviews, initiated in 1995, 1996 and 1997, respectively. UES and BSES were the only exporters involved in these reviews.<sup>2</sup>

2.7 The 1995 review, covering imports during calendar year 1994, was initiated on 14 April 1995 and was completed on 14 November 1996.<sup>3</sup> In this review, the USDOC determined a subsidy rate of 1.69 per cent on imports from UES.

2.8 The 1996 review, covering imports during calendar year 1995, was initiated on 25 April 1996 and completed on 14 October 1997.<sup>4</sup> In this review, the USDOC established two separate subsidy rates on account of the fact that UES transformed itself into BSES during the period of review. In particular, the USDOC established a subsidy rate of 2.40 per cent, applicable to imports from UES made during the period 1 January 1995 through 20 March 1995, and another subsidy rate of 7.35 per

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<sup>1</sup> Final Affirmative Countervailing Duty Determination: *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*. Federal Register, 27 January 1993, Vol. 58, No. 16, pp. 6237-6246.

<sup>2</sup> Allied Steel and Wire Limited (ASW Limited) was involved in the original 1992 investigation as well as in the 1994 review. However, this company has not participated in any subsequent reviews.

<sup>3</sup> *Certain Hot-Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*; Final Results of Countervailing Duty Administrative Review. Federal Register, 14 November 1996, Vol. 61, No. 221, pp. 58377-58383.

<sup>4</sup> *Certain Hot-Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*; Final Results of Countervailing Duty Administrative Review. Federal Register, 14 October 1997, Vol. 62, No. 198, p. 53306.

cent, corresponding to imports from BSES during the period 21 March 1995 through 31 December 1995.

2.9 The 1997 review, covering imports during calendar year 1996, was initiated on 29 April 1997 and was completed on 15 April 1998.<sup>5</sup> In this review, the USDOC determined a subsidy rate of 5.28 per cent on imports from BSES.

### **III. ARGUMENTS OF THE PARTIES**

3.1 The arguments of the parties are set out in their submissions to the Panel (see Attachments 1.1 through 1.7 for the European Communities and Attachments 2.1 through 2.8 for the United States).

### **IV. ARGUMENTS OF THE THIRD PARTIES**

#### **A. BRAZIL**

Brazil made the following written arguments as third party:

4.1 In the past decade, the US Government has issued a series of countervailing duty decisions regarding privatization. These decisions have affected, and continue to affect, a wide variety of products and countries, including Brazil. In the view of the Government of Brazil, the US Government's analysis of privatization has led consistently to countervailing measures (hereinafter CVDs) contrary to the US international obligations under the GATT 1994, and the Agreement on Subsidies and Countervailing Measures ("SCM Agreement").

4.2 The US actions and findings are inconsistent with its obligations under the SCM Agreement in two significant respects. First, the US analysis fails to recognize a duty intrinsic to Article 1 of the SCM Agreement to analyse and detect the conferral of benefits to a company during the period of investigation. This duty includes an obligation to consider all information relating to developments, such as changes in ownership, subsequent to an initial financial contribution.

4.3 The US argues that the SCM Agreement creates no duty to consider the impact of subsequent events on the flow of benefits after an initial subsidy event is detected. The US argues it can presume, irrebuttably, that the benefits of an initial subsidy event continue to flow to the new owners of an asset or company even after an arm's-length sale or privatization. This irrebuttable presumption, in and of itself, is inconsistent with the Article 1 of the SCM Agreement.

4.4 Second, given this obligation to find a benefit conferred to the company subject to investigation during the period of investigation, it is relevant how an arm's length sale affects and eliminates the conferral of benefits from a pre-sale subsidy to the purchaser. An analysis of benefit, consistent with the SCM Agreement, leads to the conclusion that a purchaser of assets (or a company) in an arm's length transaction does not receive any benefit from pre-sale infusions.

4.5 Brazil believes it important for the panel to recognize that the US Government practice impacts its CVD decisions with respect to privatizations and changes in ownership in a variety of countries, including Brazil. With respect to all forms of arm's length privatizations, the basic flaws in analysis lead to the same basic violations of SCM Agreement principles.

4.6 Brazil provides a general framework for analysing pre-privatization subsidies. This framework will assist the panel in reaching a determination that addresses the flaws in the US

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<sup>5</sup> *Certain Hot-Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, Final Results of Countervailing Duty Administrative Review. Federal Register, 15 April 1998, Vol. 63, No. 72, pp. 18367-18375.

decisions at a basic level. In this manner, the US will be forced to revise the fundamental premises of its analysis, and bring its practice for all privatization decisions into conformance with the SCM Agreement.

4.7 In addition, Brazil supplements the discussion in the First Submission of the European Communities ("EC") with additional legal analysis that applies to the underlying dispute between the US and EC, as well as other circumstances. In particular, Brazil addresses the general requirement under the SCM Agreement to identify and measure benefits of a subsidy on a basis that is specific to the company under investigation, during the period of investigation. Brazil identifies support for this requirement that supplements that addressed in the EC submission.

4.8 With respect to the impact of an arm's-length privatization, Brazil adds to the discussion in the EC submission by observing that it is always critical to focus on the "ownership relationship" between an owner and an asset (or the assets of a company in a privatization) and the terms of acquisition in determining whether a benefit exists. An examination of the owner/asset relationship is the only logical form of analysis that can support a determination that a benefit does or does not exist.<sup>6</sup> By framing its analysis in these terms, the panel's decision will address the underlying issues in this proceeding, and lay a foundation for any future consultations and disputes between the US and other WTO Members related to privatization.

## **2. Framework for analysis of pre-privatization subsidy benefits**

4.9 The question before this panel is most simply stated as whether the benefits of financial contributions made by a government or government entity to a company continue after the company that received the financial contribution has been privatized. Specifically, the question is whether the benefits of government equity infusions in government-owned companies survive the privatization of the government owned company when that privatization transfers ownership or assets to non-government entities at a fair market value.

4.10 While Article 14 of the Agreement is intended to focus on the calculation of the amount of the subsidy based on the benefit to the recipient, it is instructive in providing guidance as to what is and what is not a benefit. In terms of government provision of equity capital, paragraph (a) provides that a benefit is conferred only when such provision of equity capital is on terms "inconsistent with the usual investment practice of private investors." This benchmark of consistency with market driven policies is confirmed by paragraphs (b), (c) and (d) which all reference "commercial" or "market" criteria as the basis of determining whether a benefit has been and continues to be conferred.

4.11 With respect to some categories of benefits, the event that extinguishes the benefit is obvious. For example, if the benefit is in the receipt of below market interest on a loan from the government or a government entity, there is a benefit only so long as the loan is outstanding and the interest charged on that loan is lower than the interest that would be charged on a comparable commercial loan. Thus, the benefit ends if either the interest on the loan principal is altered to reflect commercial interest rates or if the loan itself is no longer outstanding.

4.12 The value of the benefit will, in turn, vary depending on the amount of the principal which is outstanding and the relationship between the below market interest rate and the commercial interest rate. Thus, the existence of benefits and the value of the benefits conferred can change with events which occur after the initial action by the government or government entity conferring a benefit.

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<sup>6</sup> After a change in ownership, the US applies countervailing duties primarily to pre-privatization grants and equity infusions. Thus, for the purposes of this submission, Brazil focuses on the benefits of these two forms of subsidies.



4.13 A simple example, using a pencil, illustrates how benefits and the party receiving the benefits can change over time. If a Government gives Company A a pencil, the benefit to Company A is the value of the pencil. If Company A sells the pencil at fair market value to Company B, the benefit of the Government's action still resides with Company A not Company B, since A has retained the value of the pencil in the form of cash and B has paid Company A the same amount for the pencil as it would have paid on the open market. The asset has been transferred, but the benefit remains in Company A.

4.14 Let's assume that rather than selling the pencil immediately, Company A uses half of the pencil and then sells the remaining portion of the pencil to Company B. Company B again pays fair market value, but it pays only fair market value for half a pencil since that is all it is receiving. Company B has received no benefit because it has paid market value for the pencil. Company A has a residual benefit -- the value received from Company B for half the pencil. The remainder of the benefit has been used in the form of the half of the pencil which Company A has already consumed.

4.15 Finally, assume that Company A never sells the pencil but uses it until it is finished. Under this scenario, Company A has received all of the benefits. However, after finishing the use of the pencil, no additional benefits exist. To assume benefits continue after the pencil is fully used would be to attribute benefits to Company A in terms of receiving the pencil in excess of the value of the pencil.

4.16 The analysis with respect to government provision of equity capital is really no different than the analysis of benefits where the government provides funding, goods or services at no cost or below cost to an entity. Rather than getting nothing in exchange for the funding, goods or services provided, the Government gets a share of the company and, therefore, of its assets and liabilities. In essence, it simply owns a share of the benefits received by Company A as a result of the funding, goods or services provided by the government on terms inconsistent with commercial considerations.

4.17 Let's assume, for example, that in the above example Company A is owned by the government and receives an equity investment equivalent in value to a pencil. Company A uses the equity investment to buy a pencil. Company A then sells the pencil to Company B at its market value. The benefit remains in Company A. It has simply converted a cash infusion in terms of equity into an asset and then reconverted the asset into cash by selling that asset. Company B has not received any benefit because it paid market value for the asset it acquired from Company A.

4.18 Let's further suppose that the government has decided that it no longer wants to own Company A -- i.e. it is going to privatize the company. Company A's only asset is the pencil and it has no liabilities. In the privatization, the equity shares of Company A are valued at the net of its assets and liabilities, in this case the value of the pencil. Rather than purchase the pencil itself, Company B purchases all of the equity in Company A and pays the market value of its net worth (again, the value of a pencil) to acquire the equity. Company B has received no benefit in that it has paid the fair market value for its equity purchases based on the underlying value of the company whose shares have been bought. The benefit previously conferred on Company A has been transferred to the prior shareholders in Company A through the purchase at market value of the shares in Company A. Because Company A was owned by the government, in effect the benefit has been returned to the government.

4.19 While the case being examined by the panel is more complex factually than the pencil example, the pencil example illustrates the crucial point in any analysis of benefits under the Agreement: whether you purchase an asset (the pencil) or the ownership interest in an asset (i.e. equity), neither the asset (the pencil) nor the ownership interest in the asset (the equity in the company which owns the asset) continues to have a benefit conferred on it if the new owner has paid market value for the asset or the ownership interest in the asset. The benefit remains with the original owner

of the asset or the ownership interest in the asset if the new owner pays market value to the original owner.

**2. Brazil's privatization programme was structured to eliminate pre-privatization subsidy benefits**

4.20 The privatization issue is of particular importance to Brazil, since it has undertaken a vast privatization programme, including the privatization of all formerly state-owned steel mills. The pre-privatization equity infusions to the steel mills were investigated beginning in 1983. The benefits of these equity infusions after privatization were first investigated by the US authorities in 1992/1993 and determined to remain in the privatized company. This investigation involved the first of the privatized mills, USIMINAS. The US has preliminarily reached the same conclusion in a current investigation of USIMINAS and two other privatized mills.

4.21 Ironically, the Brazilian privatization programme was structured with the specific intention of eliminating any benefits from the Government to the privatized steel mills. That is, the process devised by the Government ensured that the mills were sold at a market determined value. This result was achieved through a careful valuation process involving studies by two independent groups, the setting of minimum prices for each mill based on these studies, and the use of an auction process to ensure that market forces ultimately determined the price for each mill.

4.22 The current owners do not enjoy any benefits, having paid a market determined price for the mills. To the extent that any residual benefits of government equity infusions existed at the time of the privatization, these benefits were included in the valuation of each mill and, therefore, in the price paid. As such, no advantage was conferred on the new owners.

4.23 If pre-privatization provisions of equity capital were deemed to confer a benefit because the investment decision was inconsistent with usual investment practices as required by Article 14(a) of the SCM Agreement, then the sale of equity based on investment decisions which are consistent with usual investment practices by definition cannot confer a subsidy. In ensuring that the new owners of the mills paid a market determined price for the mills, Brazil ensured that no benefits of equity infusions in the pre-privatized companies continue to benefit the privatized companies.

**3. A plain interpretation of the provisions of the SCM Agreement requires an affirmative finding of the conferral of a benefit to a company during the relevant period**

4.24 As its initial defence, the US argues that it is not required under the SCM Agreement to recognize the absence of benefits to the purchaser of an asset or company in an arm's length transaction. At the heart of the US position is the premise that under SCM Agreement Articles 1 and 14, there is no requirement to analyse the existence and value of a benefit after the initial financial contribution. The US interpretation of Articles 1 and 14 is without support. A plain interpretation of these Articles demonstrates that the SCM Agreement requires a finding and measurement of a benefit to a company during a particular period.

4.25 Article 1 of the SCM Agreement establishes the very foundations of any determination to apply countervailing measures. As a precondition to a countervailable subsidy determination, Article 1 requires three affirmative findings:

- a financial contribution by a government (Article 1.1(a)),
- that the financial contribution thereby confers a benefit (Article 1.1(b)); and
- that the first two elements above were provided on a specific basis (Article 1.2).

4.26 The second finding involves an obligation on the part of the investigating authority to determine whether the company subject to investigation received a countervailable benefit during the period of investigation. It is not sufficient, as discussed in the EC submission, to find that a benefit is conferred to some other company, during some other period, and presume that the benefit is conceptually transferred to the company subject to investigation, and this transferred benefit is received during the period of investigation. With each company and investigation, the investigating authority is obligated to find a continuing nexus between the underlying financial contribution, and a benefit to that company during that period.

4.27 The US position relies on the view that there is no obligation to find that the firm under investigation was the recipient of the subsidy. See e.g., paragraph 156 of the US First Submission. The primary argument is that the "ordinary meaning" of Article 1 does not require a finding of benefit specific to the company subject to investigation, during the period of investigation. Rather, the US argues that Article 1 permits Members to detect and measure subsidy benefits only as of the moment of subsidization, and then allocate benefits based on that initial finding, regardless of subsequent developments.

4.28 Thus, the US position is premised on a limited interpretation of the phrase "a benefit is thereby conferred" to refer to the company that initially receives the subsidy, and the period in time when the financial contribution is initially made. The US argues that Article 1.1(b) obligates Members to find and measure the conferral of a benefit only as of the moment of the financial contribution.

4.29 The US position is in direct conflict with interpretations by the EC, Brazil and other members, that contemplates the detection of the conferral of the benefit (i.e., the continuation of the benefit) to the company subject to a particular investigation, during the relevant period of investigation. This difference in the interpretation of the intended timing of the duty under Article 1.1(b) separates the US from the EC, Brazil, and other WTO Members.

4.30 The panel should resolve this dispute as to the meaning of Article 1.1(b) by considering several relevant factors.

**4. Under the SCM Agreement, CVD investigations focus on benefits to companies during particular periods of time, regardless of the timing of the conferral of underlying subsidies**

4.31 The US is proposing an interpretation of "is thereby conferred" that is inconsistent with the mechanics and operation of the SCM Agreement, as well as other similar agreements, such as the Agreement on Implementation of Article VI of the GATT 1994 ("AD Agreement"). The US interpretation ignores the fact that CVD investigations in the US (and in most other Member countries), are company specific, and period specific.<sup>7</sup> The initial task in a CVD investigation is to focus on whether a particular company, during a particular period, benefited from subsidies. If so, the next step is to formulate a methodology that measures precisely what the benefit was during a particular period.

4.32 The ultimate objective in calculating the benefit conferred during the particular period is to identify a countervailing duty that is properly correlated to the underlying benefit. The fundamental duty at the core of Part V of the SCM Agreement - to calculate a countervailing duty that offsets no more than the benefit to a company's exports. All actions pursuant to Article 1 and 14 must be directed towards this objective. The approach proposed by the US invites an unjustified separation between the actual benefit conferred to a company during a particular period, and the calculation of a countervailing duty to be applied to the exports of that company.

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<sup>7</sup> Although more than one company may be involved in a CVD investigation, the US calculates a company-specific CVD rate for each company subject to investigation.

4.33 Interestingly, in its implementation of the SCM Agreement, US law agrees with the interpretation of the EC, Brazil and other WTO Members. Section 703(b)(1) specifically requires a determination that "a countervailable subsidy is being provided with respect to subject merchandise" (emphasis added). Thus, US law recognizes that there must be a present benefit to the specific merchandise under investigation.

4.34 Given this immediate focus on a specific period, on a specific company, the phrase "a benefit is thereby conferred" can only refer to the company subject to investigation, during the period of investigation. It does not matter if the period investigated is contemporaneous with, or significantly after, the time the actual subsidy was bestowed. The broader, more obtuse, interpretation of "is thereby conferred" advanced by the US is simply not credible.

## **5. The SCM Agreement has a bias against irrebuttable presumptions of fact over periods of time**

4.35 The US interpretation is inconsistent with other aspects of the SCM Agreement and other similar WTO agreements. The SCM Agreement, like the AD Agreement, circumscribes limited areas in which Members may make determinations, and then presume that this determination is valid for a period of time. With respect to most determinations, the SCM Agreement, like the AD Agreement, contemplates a consideration and incorporation of all relevant and current information in making a finding.

4.36 Thus, there is a pervasive bias in the SCM Agreement against presumptions that endure unchallenged over time. However, the US interpretation inserts such an unchallengable presumption in the finding of a benefit. In the underlying proceeding, the US argues that its finding and measurement of a benefit should not be revisited for 18 years, the amortization period for the benefits received by British Steel Corporation before its privatization.

4.37 The most telling example of a bias against the extended validity of a factual presumption is the requirement for regular reviews. The SCM Agreement, like the AA contemplates regular reviews of CVD findings. Such reviews are provided for in Article 21 of the SCM Agreement. In each of these reviews, the validity of the prior CVD findings is revisited. From review to review, the flow of a benefit may change, a subsidy may be withdrawn, and the value of the company's sales may change (thereby altering the ad valorem calculation), to name a few of the factors examined in a review.

4.38 The longest presumption that is permitted under the SCM Agreement is the presumption of injury. However, under SCM Agreement Article 21.3, even this presumption must be revisited at least every five years.

4.39 In this context, the unacceptability of the US suggestion that it can make a benefit flow determination at one point in time, and presume that nothing changes to interrupt this flow over a period of 15-20 years, is plain. As a result, the US position that Article 1.1 allows it to make an initial assessment of the existence and value of a benefit is inconsistent with the mechanisms contemplated by the SCM Agreement. The disciplines of the SCM Agreement require current determinations, that incorporate all of the relevant information available to the investigating authority at the time of each determination, and a valuation of such benefits at such time.

## **6. The US tries to support its interpretation of SCM Agreement Articles 1 and 14 by mischaracterizing the task of identifying and measuring a benefit to the company subject to investigation during a particular period**

4.40 The US tries to exaggerate the task and duties involved in complying with Articles 1.1 and 14. Based on this exaggeration, the US has claimed that the administration of CVD investigations under the SCM Agreement would become impossible if the EC's position is accepted. The US

position is pure hyperbole, and should be recognized as a purposeful effort to overstate the analysis required by the position advanced by the EC and Brazil.

4.41 The US complains that a "continual benefit analysis" would result in a "fundamental change" that would "seriously undermine the effectiveness of the SCM Agreement." Paragraph 22 of the US Submission. The US argues that this would require a continual inquiry into the "effects" of a subsidy.

4.42 Brazil (and presumably the EC) has never stated that a continuing "effects" test is required under Articles 1 and 14 of the SCM Agreement. As a threshold matter, an effects test suggests tracing the actual uses by a company of the financial contribution.<sup>8</sup> The EC in its first submission, and Brazil in separate proceedings, have never equated the Article 1 benefits analysis with an effects test. The benefit analysis simply examines whether the company subject to investigation enjoyed a benefit during the investigation period. An effects analysis would inquire further into how the company utilized that benefit. The panel should ensure that it does not permit the US to mischaracterize the position of Brazil, and the EC.

4.43 Second, from the standpoint of administrative burdens, the interpretation of Articles 1 and 14 is far less complicated than conveyed by the US and contrary to its current practice. Articles 1 and 14 require an affirmative determination that a benefit is conferred to the company subject to investigation, during the period of investigation. This does not entail an initial assessment, and then a "re-identification" as the US suggests. There is no "second time" that the assessment must be made. Rather, in any given investigation, the authority identifies the potential subsidy "event" in the past, and determines whether benefits flow from that subsidy to the company subject to investigation, during the period of investigation. This examination takes into consideration the initial subsidy event, and any relevant events subsequent to the subsidy event.

4.44 A countervailable loan provides a useful example. In any given investigation, in any given period, an investigating authority will identify the amount paid under the terms of the loan, and compare this to the amount that would have been paid during the same period for a loan based on market terms. However, this exercise involves an assessment of current information (i.e., what was actually paid compared to what would have been paid during the relevant period). The actual payments of the company, and fluctuations in the underlying interest rate (e.g., LIBOR), will influence the benefit to the company during the particular period. If the loan has been paid back and liquidated prior to a period of investigation, then there is no benefit during that period. As such, there is no initial benefit calculation, and then another bothersome "second" calculation. The benefit assessment for any investigation, by necessity, correlates to the period of investigation, and results in a finding specific to the company and the period of inquiry.

4.45 US practice acknowledges this need to consider subsequent events in its benefit analysis. For example, if a grant is completely repaid by a company to the government, then the US would not find that a subsidy was conferred after the repayment. As discussed above, if a loan was repaid and liquidated prior to a period of investigation, the US would not and could not find that any benefit was conferred to the company after the loan repayment. Prior to 1992, the US employed an approach of measuring the benefits of equity infusions named the "rate of return shortfall methodology." This methodology compared the rate of return of a recipient of an equity infusion with the average return for similarly situated companies. This methodology required an examination of events subsequent to the initial infusion event to determine whether a benefit was conferred during the period of investigation. All of these examples demonstrate that the US, like other Members, considers

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<sup>8</sup> For example, if a company received a grant of 1,000, an effects analysis would theoretically determine whether the company spent the 1,000 on a large unscheduled party, or if it used the 1,000 to acquire an advanced machine that directly benefited its production.

"subsequent events" in determining whether a benefit is conferred to a company during a specific period.<sup>9</sup>

4.46 The basic task in detecting a benefit is no different with respect to equity infusions. It may be necessary and appropriate to amortize certain benefits over time as an estimate of the benefits theoretically conferred during a particular period. However, the investigating member has to recognize that the benefit amortization is based on certain presumptions (i.e., that there will be no significant changes to the company or the financial contribution) and is only appropriate in certain circumstances. That is, the Member has a duty, under Article 1 and 14, to consider (and incorporate into its benefit analysis) events and developments that require it to question the presumption of an uninterrupted continuation of benefits unreasonable.

4.47 If circumstances exist, as they do after an arm's-length privatization, to undermine the use of a presumed uninterrupted benefit flow, then the investigating member simply has to tailor its analysis to the facts and circumstances of the proceeding. However, this does not involve a "first" and "second" benefit flow analysis. Rather, it simply requires the investigating member to use an appropriate analysis in the "first" instance.

4.48 In effect, the US is stating it should always invoke its uninterrupted benefit stream conclusions first, and then analyse its applicability later if requested (thereby requiring multiple benefit analysis). The EC and Brazil do not argue that this "shoot first, ask questions later" approach is required under the SCM Agreement. Their position is that, in any investigation, in detecting the existence and value of a benefit to any given company, in any given period, the investigating member must choose a form of analysis that considers all of the facts and circumstances before the authority. There is no requirement, as the US suggests, to make multiple benefit determinations.

4.49 In the privatization circumstances underlying this dispute, it is incorrect in the first instance to presume the circumstances exist to apply blindly the US benefit stream calculation. Thus, the "second" benefit analysis characterized by the US is necessary only because the first analysis did not comply with the SCM Agreement. If the US applies the correct analysis, at the outset, there is no need for multiple benefit determinations.

## **7. The SCM Agreement does not authorize members to circumvent fundamental duties and obligations due to claimed "administrative" burdens**

4.50 The US position is also problematic because it relies on a proposition unsupported by the SCM Agreement. In referring to the burdens associated with the benefit analysis proposed by the EC, the US presumes that the SCM Agreement authorizes a Member to circumvent a continual analysis of benefits to a company due to the administrative difficulties.

4.51 The determination of a benefit under Article 1, and the quantification of a benefit under Article 14, are the two most fundamental obligations under the SCM Agreement. Moreover, Article 10 states that Members "shall take all necessary steps to ensure that the imposition of a countervailing duty" is in accordance with the SCM Agreement.

4.52 Contrary to the US position, there is no offsetting provision in the SCM Agreement that authorizes a Member to sacrifice these fundamental obligations to accommodate offsetting administrative burdens on the part of the investigating Member. The US request to excuse clear duties due to administrative burdens is without support in the SCM Agreement.

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<sup>9</sup> In paragraphs 238-240 of its First Submission, the US discusses other forms of "subsequent events" it considers relevant to its subsidy benefit analysis.

**8. There is no subsidy benefit conferred on the purchaser in an arm's length sale or privatization**

4.53 Recognizing the need under SCM Agreement Articles 1 and 14 to detect and measure a benefit specific to a particular company, during a particular period, the relevant inquiry is what are the effects of a privatization or asset sale prior to the investigation period?

4.54 The position of the EC and Brazil is that under certain circumstances, the sale of an asset or company interrupts the flow of benefits to the purchaser. Specifically, when purchasers acquire a company or an asset in an arm's-length transaction, reflecting market conditions, no benefit is transferred to the purchaser as the new owner of the company. If no benefit is conferred to the owners, the company as a whole does not receive a benefit.

**9. The benefit from a grant or equity infusion relates to the receipt of assets at reduced or no costs**

4.55 Prior to the consideration of the impact of privatization, it is useful to isolate precisely the actual benefit associated with a financial contribution such as a grant or a countervailable equity infusion. The benefit of a grant or infusion is such that a company and its owners receive assets, due to government action, on terms less costly than the company would have incurred based on market conditions.

4.56 The discussion in the EC First Submission addresses this directly. See Example 1 in Paragraph 51 of the EC's First Submission. In that example, Company A receives a financial grant of 100, and then purchases a machine worth 100. The benefit to Company A is plain. Company A and its owners now have 100 in assets (either in the form of cash at the time of the infusion, or the machine after the purchase) at no cost.

4.57 The advantage to Company A derives from the terms of its acquisition of the machine. Company A obtained the machine, and now owns the machine, without the costs other companies in the market incur to obtain the same machine.<sup>10</sup> If every company in the country were given 100 (or the same machine worth 100) by the government at the same time, then there would be no countervailable benefit. It is only the comparative advantage of owning the machine worth 100 with no costs that provides the benefit.

4.58 In this sense, the analysis of the specificity requirement of a benefit in SCM Agreement Article 1.2 is linked to the requirement that the subsidy be specific.<sup>11</sup> Since Article 1.2 applies to a "subsidy," it embraces both elements of a subsidy (i.e., the financial contribution, and the benefit). Thus, a "benefit" must be specific in that it provides an advantage or privilege to a company and its owners that was not available in the market or otherwise to other companies. If same financial contribution subject to investigation is generally available to other companies, and does not thereby provide a comparative advantage to the company subject to investigation, there can be no finding of a countervailable benefit within the meaning of Articles 1 and 2 of the SCM Agreement.

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<sup>10</sup> The example changes only slightly if the original government contribution is in exchange for equity. Unlike the receipt of a grant, there are "costs" associated with the equity capital. These include the obligation of the company to respond to the demands of the government-investor for a return on its investment. In addition, the government investor retains a right to sell its shares. Thus, the benefit in these circumstances is measured by the difference between these costs, and the costs the company would have incurred but for the infusion to obtain the same 100 in capital (either by securing a loan, or issuing debt instruments).

<sup>11</sup> Pursuant to SCM Agreement Article 1, a subsidy is countervailable only if it is "specific" within the meaning of SCM Agreement Article 2.

#### **10. The same analysis of ownership relationship is appropriate after an asset is sold**

4.59 The same analysis of the terms of acquisition is required after an asset is sold in an arm's length transaction. An analysis of the dynamics of an arm's length sale of assets demonstrates that a benefit is not thereby conferred to the new owner of the asset or assets after the sale.

4.60 In the EC example 1, Company A subsequently sells the machine for its fair market value of 100 to Company B. Company B and its owners do not receive any conceivable benefit due to its ownership relationship with the machine. Company B did not acquire any economic advantage over its competitors or any other company in purchasing the machine. Thus, Company B does not enjoy any advantage in using the machine to manufacture products. In short, Company B's ownership relationship with the machine is such that it has no market advantage in acquiring, owning or operating the machine.

4.61 Although the example and analysis is plain, it is important to identify the governing principle that determines whether a benefit is conferred to Company B. It is the terms of Company B's acquisition and ownership of the machine that are dispositive in detecting a benefit. Since Company B acquired the machine at a cost no less than it (or any other company) would have paid to acquire the same machine in the market, Company B receives no competitive benefit in purchasing the machine. Its ownership relationship with the machine is such that it incurs costs equal to the costs of its competitors and other companies in the market.

#### **11. The same benefit analysis applies when all of the assets of a company are sold**

4.62 In the arm's length privatization of a company at a fair market price, the analysis is unchanged. An arm's length privatization is the sale of all of the assets (and liabilities) of a company through the sale of shares in the company. In many countries, including Brazil, a basic minimum fair value price is established above which the company must be sold.<sup>12</sup>

4.63 In an arm's length, fair market privatization, the new owners of the company compete with other potential owners for shares in the company. Ultimately, the new owners acquire shares in the company by virtue of their willingness to pay the highest price for the shares of the privatized company. Thus, the new owners in a privatization meet two conditions: they pay at least the market value for a company, and their purchase is an arm's length transaction.<sup>13</sup>

4.64 Recalling that any benefit is derived from the ownership relationship of the owner with the newly acquired asset or assets, the focus of analysis, after privatization, should be on the new owners of a privatized company, and whether they received any benefit in purchasing the company. Because the new owners paid the market value for the company, there can be no benefit to the new owners of the company.

#### **12. Arguing in the alternative, the US fails to defend its conclusion that pre-sale benefits pass through to the purchaser after an arm's length transaction**

4.65 In its submission, the US apparently recognizes that it is unlikely the panel will accept its argument that no current analysis of the benefits to a company during a particular is required under SCM Agreement Articles 1 and 14. Thus, the US argues, in the alternative, that even if a current

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<sup>12</sup> In most companies, the rights of ownership of common shares in a company are broad. They include the right to decide how to operate the assets of the company (through voting rights), the rights to company profits (through dividends), and the rights to the assets of the company if the company is sold or otherwise liquidated.

<sup>13</sup> Although the mechanics of a privatization can vary from country to country, the benefit analysis is essentially the same as long as the company is sold in an arm's length transaction, for a market determined value.



benefit analysis is required under the SCM Agreement, an arm's length sale or privatization does not eliminate the conferral of benefits to the recipient. In support for its position, the US advances three positions. All are without merit.

**13. The SCM Agreement does not focus on "productive assets" or "manufacturing" when assessing whether a subsidy benefit is conferred and received**

4.66 First, the US argues that there is an important distinction between the recipients of a subsidy (i.e., owners of a company) and the productive assets of that company at the time the subsidy is received. According to the US, "it would seem to be that the productive assets -- not the owners -- would be the determinative factor" in identifying the existence of subsidies. US Submission at 150.

4.67 Based on this, the US argues that changes in ownership of the assets are irrelevant to a subsidies analysis. Subsidy benefits somehow remain with the assets. The US position ignores the obvious flow of a benefit within a company, and ironically attempts to focus only on the "effects" of the benefit within the company.

4.68 A subsidy is clearly bestowed initially on the company, in the form of a benefit to the owners of the company. If a government provides the company with an unrestricted grant of 100, it is the owners of the company that decide how that 100 will be used.<sup>14</sup> The owners can decide to donate the 100 to charity, distribute the 100 to the directors of the company as a bonus, distribute the 100 to themselves as owners of the company, employ 10 workers for a year to do nothing productive or useful for the company (i.e., an indirect way for the government to provide social welfare benefits to its citizens), or invest the 100 in a machine to be used for future production. Thus, the owners are the direct recipient of the benefit of the subsidy. They then decide how to apply the benefit.

4.69 If the owners decide to use the subsidy to benefit the "manufacture, production, or export" of a product, then an observation can be made about the application of the subsidy benefit to the productive assets of the company. However, it would be wrong to suggest this application occurs without some initial benefit to the owners or recipients of the subsidy.<sup>15</sup> The application of the subsidy only occurs after the receipt.

4.70 Last, if the subsidy benefit is applied to manufacturing, then the products manufactured by the company are assumed to benefit from this subsidy. Ultimately, a countervailing duty is designed to offset this benefit.

4.71 The US ignores these steps from the bestowal of the subsidy to the recipient, to the presumed benefit of the subsidy to a product manufactured. The US simply focuses on the productive assets of a firm, and argues that a benefit analysis properly focuses on productive assets. This focus clearly ignores the initial steps involving the receipt and application of a subsidy. Any decision that a company is currently benefiting from a subsidy that ignores these initial steps. The US approach overlooks the essential component of a finding that a subsidy has been conferred to a company in accordance with SCM Agreement Article 1.

4.72 The US identifies several provisions in the SCM Agreement and the GATT that supposedly support its position. In particular, the US argues that SCM Agreement Articles 10 and 19.4

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<sup>14</sup> In this example, and elsewhere, the decision-makers (normally the directors and officers) of a company are presumed to be act in accordance with the direction and wishes of the owners. As a result, the example is not undermined by an observation that the directors or officers would decide how to use the subsidy.

<sup>15</sup> Ironically, in arguing that it is not required to analyse the "effects" of a subsidy, the US is acknowledging this essential relationship between the "receipt" of a subsidy, and the application of the benefit from the subsidy. The US argues it is correct to always presume that the subsidy has been applied to the production of merchandise without analysing the subsidies actual effects.

demonstrate that the focus on the SCM Agreement is on products and production and not the receipt of a benefit. The US confuses the purpose of the referenced articles.

4.73 For example, Articles 10 and 19.4 address levying duties on a "product." Clearly the application of countervailing duties is on products sold. This is the mechanism authorized by the SCM Agreement for offsetting a subsidy benefit. Articles 10 and 19.4 address this mechanism only.

4.74 However, the process of offsetting a benefit is subsequent to the initial finding of the receipt of a benefit required by Article 1. The finding of the receipt of a benefit is a precondition to the collection of countervailing duties on products exported to the investigating country. Thus, the reference to "levying duties on products" in Articles 10 and 19.4 has nothing to do with the initial finding of a benefit required by Article 1.

4.75 Similarly, the reference in Article VI of the GATT 1994 to the "manufacture, production, and export" does not support the US position. This reference clearly limits the application of countervailing duties to no more than the subsidy found to benefit the manufacture of a product. This limitation does not undermine the observation that a company and its owners must receive a subsidy before it could possibly be applied to benefit the manufacture of a product. The finding that a benefit is bestowed to a recipient (pursuant to Article 1) is a precondition to a finding that the subsidy then benefited the manufacture, production or export of a subsidy. The bestowal and receipt is required as a threshold matter to the application of countervailing duties.

**14. The SCM Agreement does not provide a mechanism to address all actions perceived by members to "distort the market"**

4.76 The US argues that a focus on the new owners of the assets sold or privatized would not take into account "market distortions" caused by the underlying subsidy. The US argues that if an arm's length transaction does not confer a benefit to the new owners and new company, then a market distortion (e.g., the creation of certain steel production capacity) will remain unredressed. The US suggests that any methodology that does not allow Members to address these macro-economic effects of a subsidy is not consistent with the objective and purpose of the SCM Agreement. Paragraph 185 of the US Submission.

4.77 This "creation subsidy" argument is based on confusion between macro-economic concerns and the disciplines and requirements of the SCM Agreement. The SCM Agreement does not provide Members with a broad-based authorization to redress actions the Member feels distort the market. Rather, it allows a Member to apply countervailing duties to the products of a particular company, during a particular period, only after certain conditions are met.

4.78 For example, if a government provided a grant of 100 to every company in its country every year, this may have market distorting effects (in the global sense) to certain industries. This 100 may be used to expand capacity in the country's steel industry (an industry the US submission describes as being plagued with overcapacity). However, since this 100 grant is generally available, there is no "subsidy" under Article 1. No countervailing duties could be applied.

4.79 The example shows that the SCM Agreement is not designed to address all forms of so-called market distortions. Part V of the SCM Agreement is intended to deal with one action only: a financial contribution, that confers a benefit to a particular recipient during a particular period analysed, on a specific basis.

4.80 The US discussion also appears to confuse injury-related analysis with Article 1 subsidy benefit analysis. In its "rental apartment" example, the US concedes that whether the purchaser of a subsidized asset receives a commercially meaningful advantage" is "open to conjecture." US Submission at paragraph 192. The US states, nonetheless, that it is important to focus on the

continuing "adverse effects" after the arm's-length sale. The Article 1 requirement of finding a benefit to the company subject to investigation authorizes no parallel consideration of the adverse effects of a prior transaction involving the assets purchased. Article 1 is far more limited, and contemplates the finding of the bestowal of a subsidy on a company subject to investigation. Any consideration of adverse effects is appropriate only within the terms of SCM Agreement Article 15.

4.81 Thus, the US "creation subsidy" argument does not provide support for its position. Instead, this argument reveals that the US privatization methodology is a practice that transcends the limitations and disciplines of the SCM Agreement. Ironically, the US rationale depends on an "effects" test, the type of test it claims the EC is relying upon, and not a "benefits conferred" test, the type of test advocated by the US

#### **15. The US wrongly interprets SCM Agreement Article 27.13**

4.82 The US argues that SCM Agreement Article 27.13 provides support for the proposition that Members may countervail prior subsidies after a privatization. US Submission, Paragraph 120 The US states that since that Article carves out an exception to when pre-privatization subsidies may be addressed, the implication is that outside that exception, pre-privatization subsidies may be addressed under both Parts III and V of the SCM Agreement.

4.83 The US acknowledges that Article 27.13 only refers to Part III. Thus, it can only be presumed that the negotiators purposefully excluded any reference Part V of the SCM Agreement. Thus, the relevance of Article 27.13 is dubious, at best.

4.84 To the extent it is relevant, it is not based on the US interpretation. Article 27.13 describes circumstances in which a Member is precluded from addressing pre-privatization subsidies of another Member. It does not follow that outside those circumstances, all pre-privatization subsidies are countervailable. Rather, the correct interpretation is that absent those circumstances, Members may investigate whether pre-privatization subsidies are passed through to the post-privatization owners.

4.85 Brazil, and presumably the EC, have never argued that a Member cannot even investigate whether pre-privatization subsidies somehow benefit the purchasers after a change in ownership. To the contrary, it is entirely appropriate to investigate the terms of the change in ownership to determine whether the sale occurred in circumstances that conferred a benefit to the new owners. As stated in the EC submission, a sale of a subsidized company at a price below its market value, in a non-competitive bidding environment, could provide the basis for a finding that the pre-sale subsidies were passed through to the purchaser. An investigation into the terms of the sale would identify this.

4.86 It is important to note, however, the distinction between the investigation of a privatization, and the automatic conclusion that the privatization conferred a benefit to the new owners. The US argues wrongly that Article 27.13 authorizes the latter conclusion. A proper legal interpretation clearly supports the first conclusion. To the extent Article 27.13 has any relevance at all to countervailing duty investigations, it is that an investigation into the form of a privatization or change in ownership is allowed in circumstances not excepted by the Article.

#### **16. Under any analysis, the US privatization "payback" methodology is flawed**

4.87 On the one hand, the US defends its privatization position by stating that it is precluded from analysing the flow of benefits from a subsidy after the government's financial contribution. On the other hand, the US does factor privatization into its CVD determination with a "payback calculation." The US payback calculation is flawed in several ways. Brazil addresses below only the most severe infirmities in the US approach.

4.88 First, the payback calculation does not analyse the actual benefits to the post-privatization company under investigation during the period of investigation. The payback calculation purports to measure the revenue "returned" to the government as a result of an arm's-length sale. However, a benefit exists only when it is determined that a person or company acquired an asset on terms inconsistent with market conditions or costs. This focus on the flow of capital to the government at the time of privatization is irrelevant to the benefit analysis discussed above.

4.89 The revenue paid to the government, and its relationship to the historical values of the government's investment, is irrelevant to the comparative benefit analysis focused on the new owners. Whether the government has, or has not, recovered the value of its investments has no impact on whether the new owners acquired their shares in the company (i.e., their right to operate the assets of the company) on a preferential basis. Even the limited privatization analysis of the US reveals that the US focuses wrongly on circumstances irrelevant to a benefit determination.

4.90 Second, to the extent payback is relevant, the US payback approach relies unjustifiably on the crude assumptions of a benefit stream calculation. The actual fair value of a company (or asset) provides information far more precise and useful in determining the value of subsidy benefits theoretically still embedded in the company at the time of privatization. The US methodology assumes it can identify the amount of subsidies repaid to the government through its calculations of gamma, and the net present value of all unamortized subsidies.

4.91 If a company or asset is sold at market value, however, this market value necessarily includes and reflects the actual (if any) benefits still remaining with the company at the time of privatization. A market value sale will, by definition, reflect the full value of the company, including all benefits residing with the company at the time of privatization. In this regard, the market value sale of the company or asset will necessarily result in the payback of all subsidy benefits still residing with the company at privatization to the government. Rather than employing the market analysis of the company (reflected in its privatization price), the US wrongly believes that its benefit stream amortization methodology, along with its gamma calculation, more accurately determine the value of the residual subsidies in the company at the time of privatization.

4.92 The US payback methodology provides additional evidence that the US analysis of privatization is inconsistent with the SCM Agreement because it does not focus on the benefit to the recipient, and fails to incorporate correctly market value information in determining a payback to the government as a result of privatization.

**17. Pursuant to the standards of review of the dispute settlement understanding, the Panel should not accord any deference to US actions in determining whether the US has acted inconsistently with its obligations under the SCM Agreement.**

4.93 The underlying dispute involves the application of countervailing duties under Part V of the SCM Agreement. Article 30 of the SCM Agreement dictates that the terms and provisions of the Dispute Settlement Understanding (DSU) apply to all disputes under the SCM Agreement. The panel's duty under the DSU is to determine whether there is an infringement of the obligations assumed under the relevant agreement. See e.g., Article 3.8 of the DSU.

4.94 In making this determination, this panel is not authorized to provide any deference to the permissibility of the US actions. That is, the standard of review described in Article 17.6 of the AD Agreement does not apply to these proceedings.

4.95 Article 17.6 was purposefully included in the AD Agreement, and at the same time purposefully excluded from the SCM Agreement. This is clear from the principle of interpretation cited by the US in their submission - *inclusio unius est exclusio alterius* (the inclusion of one is the exclusion of another). If the negotiators of the SCM Agreement intended the Article 17.6 standard of

review to apply to disputes arising from the SCM Agreement, they would have included this standard of review in the SCM Agreement.

4.96 The US argues that the Declaration on Dispute Settlement Pursuant to the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 or Part V of the Agreement on Subsidies and Countervailing Measures from the Uruguay Round "Declaration") provides support for the proposition that the AA Article 17.6 standard applies to disputes arising from the SCM Agreement.

4.97 The legal analysis of the US is skewed. First, the very existence of the Declaration demonstrates that there was, and is, a current disparity in the standards of review between the SCM Agreement and the AA. If they were equivalent after the Uruguay Round, there would be no need for the Declaration. The Declaration represents a "need" for consistent resolution, despite the fact that the two agreements (after the Uruguay Round) had distinct standard of reviews. Thus, the Declaration reflects an intention and a pledge to take future action to resolve this disparity. The Declaration, however, does not govern the actions of the panel. If it did, the Declaration would have been included as an article in the DSU.

4.98 Second, the US interpretation of the meaning of the Declaration is flawed. The Declaration simply states the need for a consistent resolution of disputes arising from anti-dumping and countervailing duty measures. It does not follow, however, that the WTO Members will ultimately decide this in favor of the Article 17.6 standard. It is equally possible that some other standard will be developed that will apply equally. This could include, among other things, the normal standard of the DSU. In short, there is no reason for this panel to presume or speculate whether the WTO Members will ultimately act on the Declaration, and if so, what uniform standard the Members will propose and adopt. In the interim, this panel must follow the dispute resolution terms in the SCM Agreement and DSU that govern this dispute.

4.99 For all of the foregoing reasons, the panel should find that the US has acted inconsistently with its obligations under the SCM Agreement. The US analysis of privatization is contrary to its obligations under SCM Agreement Articles 1 and 14 to find a benefit conferred to a company subject to investigation.

## B. MEXICO

Mexico made the following written arguments as third party:

4.100 Since the middle of the 1980s, Mexico has been pursuing an extensive privatization policy as part of its economic development programme. Mexico remains convinced of the importance of privatization and has maintained its efforts to that end, permitting and ensuring domestic and foreign investment in all kinds of public enterprises.

4.101 Unfortunately, the United States policy of applying countervailing duties to companies that are privatized has caused great concern to the owners of the companies in question and to potential investors. Not only is the uncertainty caused by this policy directly affecting the confidence of investors and reducing the real value of public enterprises, it is unfair to investors who have made bids for these assets.

4.102 The new United States regulations on subsidies maintain the policy applied by the country's authorities and tribunals whereby when a public enterprise is privatized, the benefits deriving from subsidies granted by the State are not extinguished. The investigating authority has considerable

discretion in determining how the share of the subsidy that "subsists" following privatization is distributed. This regulation corresponds to a practice which has already affected Mexico in the past.<sup>16</sup>

4.103 In the statement of reasons for the regulations, the DOC reviews various comments, including some that were made to the DOC by the Government of Mexico. The DOC qualifies the position that a privatization may extinguish the benefits of a subsidy as extreme. The DOC states that the definition of subsidy under United States law does not require it to determine whether and how a benefit exists following privatization, but only to make a determination at the point in time when the benefit was granted.

4.104 In general, the DOC's position on privatization could affect future exports of Mexican enterprises that have been privatized or are to be privatized. In particular, exports of carbon steel plate by the company Altos Hornos de México, S.A. (AHMSA) are currently seriously affected by the United States' maintenance of countervailing duties on account of subsidies granted prior to the company's privatization.

4.105 According to the letter and objectives of the Agreement on Subsidies and Countervailing Measures (ASCM), the application of countervailing duties must be transparent and based on the principle whereby an investigating authority must presume that privatization carried out between unrelated persons and at market value necessarily puts an end to any benefit granted prior thereto, and that it is up to the party claiming the contrary to prove how a financial contribution continued following privatization and specifically identify the benefit granted.

## **1. General observations**

4.106 Mexico observes that some of the United States' arguments are based on its domestic legislation.<sup>17</sup> To justify this, the United States asserts that "it is an accepted principle of international law that municipal law and practice is a fact to be proven before an international tribunal, such as this Panel."<sup>18</sup> At the same time, it accepts that "US court decisions ... are in no way binding on a WTO panel".<sup>19</sup> Mexico contends that interpretations by the United States tribunals of its domestic legislation are entirely irrelevant to this case, since they do not constitute precedent<sup>20</sup> for the Panel, much less "interpretations" under the Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement).<sup>21</sup>

4.107 Moreover, the United States tries to justify its methodology for applying countervailing duties under Article 17.6 of the Anti-Dumping Agreement.<sup>22</sup> Mexico considers that the fact that the Ministers recognized the need to ensure coherence in dispute settlement between anti-dumping measures and countervailing measures does not necessarily imply that Article 17.6 applies *mutatis mutandis* to the ASCM. The provisions of the Anti-Dumping Agreement are unique to that

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<sup>16</sup> See first submission of the EC, 27 April 1999, paragraphs 5-27, in particular 5-11, 26 and 27.

<sup>17</sup> First submission by the United States, 18 May 1999, in particular paragraphs 36-61.

<sup>18</sup> *Ibid*, footnote 8.

<sup>19</sup> *Ibid*, paragraph 61.

<sup>20</sup> In the case *Japan – Taxes on Alcoholic Beverages* (WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R), adopted on 28 November 1996, the Appellate Body found on page 18 of its report that since adopted reports were not binding except with respect to resolving a particular dispute, they should be taken into account when they were relevant to a dispute, and unadopted panel reports could provide useful guidance when they were relevant to the case at issue. In this case, we are dealing neither with panel reports prepared in the framework of the WTO dispute settlement mechanism, nor with disputes within the framework of the ASCM.

<sup>21</sup> Article IX.2 of the WTO Agreement limits the exclusive authority to adopt interpretations of the Agreement on Subsidies and Countervailing Measures to the Ministerial Conference and the General Council.

<sup>22</sup> See first submission of the United States, paragraphs 102-105.

Agreement<sup>23</sup> and so long as Article 17.6 is not expressly incorporated in the text of the ASCM, the Panel is under no obligation to apply it.

## 2. Legal arguments

4.108 It is Mexico's understanding that the matter submitted to this Panel includes, inter alia, the following aspects of United States policy in respect of countervailing duties:

- Refusal to take account of "the privatization or change of ownership of the body receiving a subsidy, even if at a full market price, and to consider whether the subsidy still provides a benefit when assessing or reassessing the countervailable subsidy. Instead, the United States considers that the subsidy 'travels with' the assets when they are transferred."<sup>24</sup>
- Failure to justify or rationalize in the final determinations "what benefits continue to result from subsidies following privatization or a sale of assets at fair market prices."<sup>25</sup>

4.109 Mexico agrees with the EC and supports the arguments that the United States violated Article 10 of the ASCM in conjunction with Articles 19.1 and 14 of the ASCM, as well as Article VI of the GATT 1994, by imposing countervailing duties without first establishing whether there existed any subsidy.<sup>26</sup>

4.110 Similarly, Mexico agrees with the EC's position that even if there were a subsidy, the amount of that subsidy would be equivalent to zero, so that the application by the United States of any countervailing duty greater than that amount is "in excess of the amount of the subsidy" and violates Article 19.4 of the ASCM.<sup>27</sup>

4.111 It is our understanding that the United States' arguments are basically as follows:

- The ASCM is silent on the question of privatizations, so that the Panel must accept as "permissible" the interpretations made by the United States of that Agreement<sup>28</sup>;
- the investigating authority is required to determine the existence of subsidies, and ultimately, of benefits, only once;
- the subsidies affect the market in such a way that even if the company changes hands, they will continue to cause injury to the domestic industry of the importing Member.

4.112 Regarding the first of these arguments, Mexico contends that the ASCM does not need to expressly include the word "privatization". It is clear from the text of the Agreement that it regulates, inter alia, the application of countervailing duties in general. In other words, it regulates the

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<sup>23</sup> In examining the concept of "measures" in the framework of the Anti-Dumping Agreement, the Appellate Body in the case *Guatemala - Anti-Dumping Investigation Regarding Portland Cement from Mexico* found, in paragraph 79 of its Report (WT/DS60/AB/R) adopted on 25 November 1998, that Article 17.4 of the Anti-Dumping Agreement specified three types of anti-dumping measures: definitive anti-dumping duties, the acceptance of price undertakings, and provisional measures, adding that "we note that the language of Article 17.4 of the Anti-Dumping Agreement is unique to that Agreement."

<sup>24</sup> Request for the Establishment of a Panel by the European Communities (WT/DS138/3).

<sup>25</sup> Corrigendum to the Request for the Establishment of a Panel by the European Communities (WT/DS138/3/Corr.1).

<sup>26</sup> First written submission of the European Communities, in particular paragraphs 81-118.

<sup>27</sup> *Ibid*, paragraphs 119-138, particularly paragraph 119.

<sup>28</sup> First submission of the United States, particularly paragraphs 107 and 148.

procedure that an investigating authority must follow to that end. It is well known that the investigating authority is required to examine all of the elements enabling it to determine whether (i) through the effects of (ii) a subsidy there is (iii) injury to a domestic industry.<sup>29</sup>

4.113 Article 1.1 of the ASCM states that a "subsidy" shall be deemed to exist if there is a financial contribution by a government or any public body within the territory of a Member and a benefit is thereby conferred. In other words, in order to be able to apply a countervailing measure it is necessary first to determine that there is a subsidy. To determine that there is a subsidy, a benefit must be conferred. Thus, if there is no benefit, a Member is not entitled to apply a countervailing measure. That is, in principle, the contribution was extinguished upon privatization of the entity. The investigating authority cannot assume that the said contribution "travels with" the purchasing enterprise.

4.114 In a transaction between an independent, rational and informed seller and buyer, each looking after its own interest, the price of the transaction necessarily corresponds to its market value. For example, in the case of Mexico, the privatization of AHMSA took place by public tender.

4.115 Where an enterprise has been privatized at a price which corresponds to its full market value, this necessarily corresponds to the total price of the enterprise, including any advantage or benefit it may have. In other words, the market value paid absorbs the benefit that would have been conferred on the said enterprise, and the benefit therefore ceases to exist.

4.116 As regards the second argument, the United States asserts that in their ordinary meaning, subparagraphs (a) and (b) of Article 1.1 (drafted in the present tense) indicate that the investigating authority is not required to make a new benefit determination simply because the ownership of the original subsidy recipient has changed hands.<sup>30</sup>

4.117 Mexico does not agree with this reasoning, since the foundation on which it rests is incorrect. To assume, as the United States has done, that the fact that Article 1.1 is drafted in the present tense provides sufficient reason to presuppose that the investigating authority is only required to make a finding of a subsidy benefit once, is to ignore the general context of the ASCM. Firstly, according to Articles 11, 17.1(b) and 19.1 of the ASCM, the determination that a subsidy exists must be made at least three times: on initiating the investigation, on making the preliminary determination and on making the final determination. That is, the investigating authority is required to determine the existence of a subsidy at least three times.

4.118 Moreover, Article 21 stipulates that a countervailing duty shall remain in force only as long as and to the extent necessary to counteract subsidization, and confers the right to request the authorities to examine whether the continued imposition of the duty is necessary to offset subsidization. This means that the authority must determine, for each examination, the existence of a subsidy – otherwise it will be unable to establish whether it is necessary to maintain the duty in order to offset the subsidy.

4.119 At the same time, Article 27.13 of the ASCM provides for benefits for developing country Members (such as Mexico) by not applying the provisions of Part III to direct forgiveness of debts or subsidies to cover social costs "when such subsidies are granted within and directly linked to a privatization programme". The United States argues in this connection that the wording of this article implies that all other privatizations are subject to subsidization.<sup>31</sup> This does not apply, however, to the case of the United Kingdom presented by the EC and certainly does not apply to the case of AHMSA,

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<sup>29</sup> Articles 17.1(b) and 19.1 in particular.

<sup>30</sup> First submission of the United States, paragraphs 118 and 120. Mexico notes that the Spanish text of Article 1.1(a) and (b) of the ASCM is not drafted in the present tense, but in a subjunctive. This point is repeated in paragraphs 137 to 139, 149 and 156-158.

<sup>31</sup> *Ibid*, paragraphs 151-160.



since these are not cases of subsidies granted within or directly linked to a privatization programme. Moreover, this provision excludes, by definition, the notion of "market value", so that the United States' interpretation whereby "to specify one thing is to exclude the other" is not applicable.

4.120 Finally, the United States asserts that subsidies do not apply to specific persons, but to the production or sale of products.<sup>32</sup> Similarly, it admits that it has been the practice of the United States Department of Commerce (USDOC) that subsidies can be extinguished by being repaid to the government<sup>33</sup>, and subsequently admits that the amount of the purchase price simply affects the allocation of subsidies between seller and purchaser.<sup>34</sup> Lastly, it provides an example which implies that a subsidy affects the market irreversibly.<sup>35</sup>

4.121 These assertions by the United States are erroneous, since they are based on the assumption that the operation of a public enterprise follows a defined path, that it is only briefly affected for the purpose of the privatization and that it then continues its operations as though nothing had happened. They do not take account of the fact that like any other asset of the enterprise, a benefit (which may have taken the form of an industrial plant, machinery or equipment, or means of transport) has a determined price and that the purchaser that has paid the market price for the company (including the benefit) will want to recover the investment and generate profits. To that end, the purchaser may take decisions on production, operation and sales that differ completely from those taken by the company when it belonged to the government.

4.122 Furthermore, when a public enterprise is privatized and the purchaser pays the enterprise's market price, the seller (the government) in fact receives the money that the enterprise was worth, with all of its assets.

4.123 Finally, the United States' example concerning the rich uncle buying a building could be perfectly applicable even if the nephew had bought the building with his own money. It is because the supply has increased and the prices have gone down that there is a new building available to the public, and not because that building was bought by a rich uncle.

### **3. Conclusions**

4.124 Although the ASCM does not expressly address the question of privatization, the United States' interpretation of the Agreement is inconsistent with both its letter and objectives, since the privatization of companies at arm's length and at market value absorbs the benefits previously conferred on that company.

4.125 In order to apply countervailing duties under the ASCM, the investigating authority is required to examine whether there are subsidies, and ultimately, benefits. This examination may take place at the initiation of the investigation or upon making a provisional or final determination, or even thereafter, upon examining whether it is necessary to maintain the duties.

4.126 The United States violated Article 10 of the ASCM by applying countervailing duties without complying with the provisions of the ASCM itself.

4.127 Even if there had been a subsidy, it would have been equivalent to zero, so that the United States violated Article 19.4 of the ASCM by applying a higher duty.

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<sup>32</sup> *Ibid*, paragraphs 9 and 204.

<sup>33</sup> *Ibid*, paragraph 47.

<sup>34</sup> *Ibid*, paragraph 55.

<sup>35</sup> *Ibid*, paragraphs 223-225.

## **V. INTERIM REVIEW**

5.1 On 6 October 1999, the Panel issued its interim report to the parties. On 20 October 1999, the European Communities and the United States requested the Panel to review precise aspects of the interim report, in accordance with Article 15.2 of the DSU. Neither party requested an additional meeting with the Panel.

### **B. COMMENTS BY THE EUROPEAN COMMUNITIES**

5.2 The European Communities requested changes to the Panel's description of the European Communities' arguments in paragraphs 6.12, 6.36 and 6.71. We have made certain modifications to paragraphs 6.12, 6.36 and 6.71.

5.3 The European Communities requested replacing the word "effectively" in the penultimate sentence of paragraph 6.57 with the word "therefore". Because we consider the word "effectively" appropriate in this context, we decline to make the modification requested by the European Communities.

5.4 The European Communities requested the addition of certain references to footnote 66, in order to include all references where the parties have discussed the term "deter". In our view, the references we have cited in footnote 66 constitute the clearest statement of the US position on whether countervailing duties should be applied to deter subsidization. Since it is the position of the United States on this matter to which footnote 66 refers, we decline to make the modification requested by the European Communities.

5.5 The European Communities requested the Panel to include the terms "of a developing country Member" in the second sentence of footnote 86. Given the explicit wording of Article 27.13 of the SCM Agreement, we have modified footnote 86 in line with the European Communities' request.

5.6 The European Communities requested the Panel to replace the term "conferred" with the term "bestowed" in the second sentence of paragraph 6.80, to avoid confusion and to bring this sentence in line with the terminology used by the Panel elsewhere in its report. We have modified the second sentence of paragraph 6.80 accordingly.

5.7 With regard to paragraph 8.1, the European Communities requested the Panel to also recommend that the United States bring its treatment of pre-privatization subsidies into conformity with the SCM Agreement. Since our terms of reference are restricted to those measures cited by the European Communities in document WT/DS138/3 and WT/DS138/3/Corr. 1, we decline to make the modification requested by the European Communities.

### **C. COMMENTS BY THE UNITED STATES**

5.8 The United States requested the Panel to modify paragraphs 6.24, 6.26, 6.60, 6.61 and 6.62, to reflect the distinction between the USDOC's 27 January 1993 final determination and the USDOC's 12 October 1993 remand determination. We have made certain changes to the aforementioned paragraphs.

5.9 The United States requested a modification in the second sentence of paragraph 6.25, concerning the duration of the allocation period. We have modified the second sentence of paragraph 6.25 accordingly.

5.10 The United States requested a correction concerning the identification of the Attachment referenced in footnote 66. We have corrected that reference.

5.11 The United States asked the Panel to include a fuller description of its argument in footnote 66. We have modified our description of the US argument in footnote 66.

5.12 With regard to paragraph 6.59, the United States requested certain modifications to the Panel's description of the US position regarding the existence of "benefit". The United States considered the Panel's description incomplete and disjointed. We note that the language used by the Panel to summarize the US position on the existence of "benefit" is taken from a US submission (Attachment 2.1), and that the United States would simply have the Panel include an extended description of the US position on the existence of "benefit" taken from the same US submission. Since the United States has not demonstrated that our summary of the US position is inconsistent with the arguments made by the United States before this Panel, we decline to make the changes requested by the United States. Any reader wishing to read a complete description of the US arguments on this matter may consult the original US submission, which is explicitly cross-referenced by the Panel at paragraph 6.59.

5.13 The United States requested the Panel to make technical corrections in footnote 75. We have modified footnote 75 accordingly.

## **VI. FINDINGS**

### **A. INTRODUCTION**

6.1 On 22 March 1993, the US Department of Commerce ("USDOC") published a countervailing duty order imposing countervailing duties on imports of leaded bars originating *inter alia* in the United Kingdom ("UK").<sup>36</sup> The USDOC initiated administrative reviews of that order in 1994, 1995, 1996, 1997, 1998 and 1999. This dispute concerns the consistency with Articles 10 and 19.4 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") of the countervailing duties imposed as a result of the administrative reviews initiated in 1995, 1996 and 1997.

### **B. PRELIMINARY ISSUES**

#### **1. Participation of observers**

6.2 By letter dated Friday, 11 June 1999, the United States asked the Panel to allow observers to attend the Panel's meetings with the parties. In response, the Panel issued the following decision at the first substantive meeting with the parties:

#### **DECISION CONCERNING THE US REQUEST FOR PARTICIPATION BY OBSERVERS**

By letter dated Friday, 11 June 1999, the United States asked the Panel to allow observers to attend the Panel's meetings with the parties. The Panel notes that the US request was submitted only one full working day before the first substantive meeting of the Panel with the parties on Tuesday, 15 June 1999. The Panel regrets that the United States was not able to submit its request in a more timely manner.

By letter dated Monday, 14 June 1999, the Panel sought the views of the EC, Brazil and Mexico on this matter. In separate written responses dated 14 June 1999, the EC, Brazil and Mexico asked the Panel to reject the US request. The Panel is grateful for the speed with which the EC, Brazil and Mexico were able to provide their views on this matter.

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<sup>36</sup> 58 Fed. Reg., p. 15327 (hereinafter "1993 *Leaded Bars* duty order").

We note that, in accordance with paragraph 2 of the Panel Working Procedures contained in Appendix 3 of the DSU ("Appendix 3 Working Procedures"), "[t]he panel shall meet in closed session." Whereas paragraph 2 refers to the presence of the "parties to the dispute" and "interested parties"<sup>37</sup> at panel meetings, paragraph 2 does not refer to the presence of observers. For this reason, we consider that participation by observers at panel meetings would be inconsistent with paragraph 2 of the Appendix 3 Working Procedures.

Article 12.1 of the DSU provides that a panel is entitled to depart from or add to paragraph 2 of the Panel Working Procedures, after consulting the parties to the dispute. In *United States - Import Prohibition of Certain Shrimp and Shrimp Products*, the Appellate Body explained that:

" ... Article 12.1 of the DSU authorizes panels to depart from, or add to, the Working Procedures set forth in Appendix 3 of the DSU, and in effect to develop their own Working Procedures, after consultation with the parties."

Article 12.1 of the DSU requires a panel to consult with the parties before developing its own Working Procedures. Article 12.1 does not expressly require a panel to seek the agreement of the parties to the dispute before developing its own Working Procedures. However, in certain circumstances such agreement would appear appropriate. This is especially so with regard to the participation of observers, as a result of possible implications for the confidentiality of parties' oral statements to the panel.

Paragraph 3 of the Appendix 3 Working Procedures provides that "documents submitted to [the panel] shall be kept confidential." Paragraph 3 does not refer to the confidentiality of oral statements made by parties during meetings with the panel. However, to the extent that a party's oral statement refers to, or repeats, all or part of its written submission to the panel, a failure to protect the confidentiality of a party's oral statement could effectively undermine the confidentiality of its written submission.

By virtue of paragraph 3 of the Appendix 3 Working Procedures, a party may forego the confidentiality of its written and oral submissions by "disclosing statements of its own position to the public." We note that it is up to each party to decide whether it wishes to forego the confidentiality of its submissions to the panel. This is not a decision to be made by a panel. Since it is up to each party to decide whether or not it chooses to forego its right to confidentiality for its written and oral submissions to a panel, we are obliged to seek the agreement of each party before implementing Working Procedures that might undermine the confidentiality of a party's written and oral submissions. By its 14 June response to the US request of 11 June 1999, the EC effectively withheld such agreement. As a result, we are not in a position to develop any Working Procedures that might jeopardise the confidentiality of the EC written and oral submissions to the Panel. Accordingly, we are unable to grant the US request to open this meeting to observers.

## **2. Amicus curiae brief**

6.3 On 19 July 1999, we received a brief from the American Iron and Steel Institute ("AISI") dated 13 July 1999. We note that, by virtue of Articles 12 and 13 of the DSU, a panel "has the discretionary

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<sup>37</sup> In our opinion, the term "interested parties" refers to third parties, *i.e.*, "parties which have notified their interest in the dispute to the DSB" (paragraph 6, Appendix 3 Working Procedures).

authority either to accept and consider or to reject information and advice submitted to it, *whether requested by a panel or not*."<sup>38</sup> While we clearly have the discretionary authority to accept the AISI brief, in this case we chose not to exercise that authority as a result of the late submission of the brief. The AISI brief was submitted after the deadline for the parties' rebuttal submissions, and after the second substantive meeting of the Panel with the parties. Thus, the parties have not, as a practical matter, had adequate opportunity to present their comments on the AISI brief to the Panel. In our view, the inability of the parties to present their comments on the AISI brief raises serious due process concerns as to the extent to which the Panel could consider the brief. In accordance with Article 12.1 of the DSU, the Panel may have been entitled to delay its proceedings in order to provide the parties sufficient opportunity to comment on the AISI brief. However, we considered that any such delay could not be justified in the present case.

### 3. Request for information

6.4 In its written response to a question from the Panel,<sup>39</sup> the European Communities requested the Panel to "ask the United States to provide all parties with [the] facts [surrounding the Richemont spin-off in *Stainless Steel Sheet and Strip in Coils from France*]<sup>40</sup>, including: (1) the essential USDOC spin-off calculation worksheets containing all the specific numbers that led to the conclusions drawn by USDOC regarding the spin-offs in the case, and (2) all supporting memorandums, including the portion of the verification report dealing with Richemont cited by the USDOC at 64 Fed. Reg. 30776."

6.5 In response to a separate question from the Panel, the United States asserted that such information "was submitted ... as business proprietary information, and USDOC is therefore precluded by U.S. law from divulging it."

6.6 We note that, by virtue of Article 13 of the DSU, a panel has authority to seek information and technical advice from "any individual or body" it may consider appropriate, or from "any relevant source." The "comprehensive nature" of this authority was emphasised by the Appellate Body in *United States - Shrimp*.<sup>41</sup> In *Canada - Measures Affecting the Export of Civilian Aircraft*, the Appellate Body explicitly stated that a panel has the authority to seek information from "any Member, including *a fortiori* a Member who is a party to a dispute before a panel."<sup>42</sup>

6.7 Thus, if we consider it appropriate, there is no doubt that we have the authority to request information concerning the Richemont spin-off from the United States. In particular, we are not persuaded that the proprietary nature of the information precludes us from requesting (or the United States from submitting) the information, since it is open to the Panel to implement special procedures to protect proprietary information.<sup>43</sup> However, we do not consider it necessary to request the relevant information from the United States. In our view, the present dispute can be resolved without reference to the precise facts surrounding the Richemont spin-off in *Stainless Steel Sheet and Strip*. For this reason, we decline to exercise our authority under Article 13 of the DSU to ask the United States to provide the information sought by the European Communities.

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<sup>38</sup> *United States - Import Prohibition of Certain Shrimp and Shrimp Products* (hereinafter "*United States - Shrimp*"), WT/DS58/AB/R, adopted 6 November 1998, para. 108.

<sup>39</sup> See Attachment 1.3, Question 3.

<sup>40</sup> *Stainless Steel Sheet and Strip in Coils from France*, 64 Fed. Reg. 30774, 8 June 1999 (hereinafter "*Stainless Steel Sheet and Strip in Coils from France*").

<sup>41</sup> *United States - Shrimp*, WT/DS58/AB/R, adopted 6 November 1998, para. 104.

<sup>42</sup> *Canada - Measures Affecting the Export of Civilian Aircraft* (hereinafter "*Canada Aircraft*"), WT/DS70/AB/R, adopted 20 August 1999, para. 185.

<sup>43</sup> We note that such special procedures were implemented by the *Canada Aircraft* panel (WT/DS70/AB/R, adopted 20 August 1999, Annex 1).

#### 4. Standard of review

(a) The United States

6.8 The United States asserts that the standard of review set forth in Article 17.6 of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (hereinafter the "AD Agreement") is expressly made applicable to disputes under the SCM Agreement by virtue of the Ministerial Declaration on Dispute Settlement Pursuant to the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 or Part V of the Agreement on Subsidies and Countervailing Measures (hereinafter "Ministerial Declaration"), which refers to "the need for consistent resolution of disputes arising from anti-dumping and countervailing duty measures." The United States argues that this Ministerial Declaration "must have some meaning". In the United States' view, Members were aware of the many similarities between the anti-dumping proceedings and the countervailing duty proceedings that a panel would be reviewing, and they did not want inconsistent resolutions for disputes under the AD Agreement and the SCM Agreement simply because of the use of different standards of review. According to the United States, the import of the Ministerial Declaration is that a panel should use the AD Agreement's standard of review when reviewing a countervailing duty proceeding.

6.9 In response to a question from the Panel regarding the Ministerial Decision on Review of Article 17.6 of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (hereinafter "Ministerial Decision"), the United States asserts that the Article 17.6 standard of review does not apply to the present dispute by virtue of the "general application" of that provision. Accordingly, the United States argues that the Ministerial Decision is not relevant in this dispute.

6.10 In the event that the Panel finds the standard of review set forth in Article 17.6 of the AD Agreement inapplicable to this dispute, the United States accepts that the Appellate Body's decision in *European Communities - Measures Concerning Meat and Meat Products*<sup>44</sup> states the applicable standard of review, i.e., that set forth in Articles 3.2 and 11 of the DSU. However, the United States asserts that the *Hormones* decision does not represent a complete statement of the standard of review that must be applied by the Panel in this dispute. In particular, with regard to legal questions, the *Hormones* decision explains only that a panel must apply the customary rules of interpretation of public international law. It does not address what a panel should do in the situation where, as in the present case, the agreement at issue is silent with regard to a particular matter even after applying the customary rules of interpretation of public international law. According to the United States, the key provision in the SCM Agreement -- Article 1.1 -- is silent regarding how an investigating authority is to handle previously bestowed subsidies following a change in the ownership of the subsidized company.

6.11 The United States submits that, when the SCM Agreement is silent, a panel addressing a dispute under Part V of the SCM Agreement should follow either *United States - Imposition of Countervailing Duties on Imports of Fresh and Chilled Atlantic Salmon from Norway*, where the panel stopped its analysis and found the challenged approach to be not inconsistent with the relevant agreement after determining that the agreement was silent,<sup>45</sup> or *New Zealand - Imports of Electrical Transformers from Finland*, where the panel took a slightly different approach and found no violation

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<sup>44</sup> *European Communities - Measures Concerning Meat and Meat Products* (hereinafter "*Hormones*"), WT/DS26/AB/R, WT/DS48/AB/R, adopted 19 February 1998, at paragraphs 114-19.

<sup>45</sup> *United States - Imposition of Countervailing Duties on Imports of Fresh and Chilled Atlantic Salmon from Norway* (hereinafter "*United States - Salmon*"), adopted 28 April 1994, BISD 41S/576, at paras. 243-46 and 247-49.

of the relevant agreement after concluding that the approach used by the investigating authority “appeared to be a reasonable one.”<sup>46</sup>

(b) The European Communities

6.12 The European Communities objects to the application of the standard of review set forth in Article 17.6 of the AD Agreement to the present case. The European Communities asserts that Articles 3.2 and 11 of the DSU set the standard of review applicable in this dispute. The European Communities takes issue with the US interpretation of the Ministerial Declaration, asserting that a “consistent resolution” of disputes does not allow for an “adoption” of Article 17.6 of the AD Agreement in a different Agreement than for which it was written. The European Communities argues first that Ministerial Declaration is not a covered agreement and therefore not within the Panel’s mandate; it is more in the nature of a reminder to negotiators to aim for consistency between the Antidumping and Countervailing Duty provisions. In any event, the EC submits that any meaning it has is much more limited, requiring only that parallel provisions in the two Agreements should be dealt with in a consistent way. For example, an allegation that an investigating country had exceeded the maximum 18 months for an investigation should not be treated differently in anti-dumping and countervailing duty cases.<sup>47</sup> The European Communities asserts that taking the far-reaching step of adopting textual provisions into an Agreement which are not there would “add to or diminish the rights and obligations provided in the covered agreements”, and would therefore violate Article 3.2 DSU.

6.13 The European Communities submits that there is no ground for ignoring the text of the Ministerial Decision and the United States offers none. The text of the Ministerial Decision is clear, in that it should be decided at a later time whether or not Article 17.6 of the AD Agreement could be capable of “general application”. The European Communities believe that the ordinary meaning of the term “general application” is the “use outside the Anti-Dumping Agreement”, or the “use in all other covered agreements of the WTO”. The text of the Ministerial Decision does not contain any preferential treatment for the SCM Agreement, which would somehow allow the adoption of the 17.6 standard already at this moment in time in the SCM Agreement.

6.14 The European Communities denies that the SCM Agreement is “silent” on the key issues in dispute, since the SCM Agreement is not “silent” on the fundamental obligation of a Member to establish the existence of a “benefit”, and therefore a “subsidy” which may be “offset” by countervailing duties, to the company under investigation. The European Communities also argues that there is no room for a reliance on the two pre-WTO cases referred to by the United States, since they concern only technical factual calculations by national authorities in areas in which the relevant GATT Codes were silent. As such, the European Communities believes that these cases are particularly lacking in relevance in the present case, where a fundamental precept of the SCM Agreement is at issue.

(c) Evaluation by the Panel

6.15 The United States advocates the application of the standard of review set forth in Article 17.6 of the AD Agreement. Given the nature of the present dispute, it is in particular the standard of review set forth in paragraph (ii) of Article 17.6 which the United States would have us apply. Article 17.6 (ii) of the AD Agreement provides:

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<sup>46</sup> *New Zealand - Imports of Electrical Transformers from Finland* (hereinafter “*New Zealand - Transformers*”), adopted on 18 July 1985, BISD 32/S55, at paras. 4.2-4.3.

<sup>47</sup> Thus, the European Communities asserts for example that disputes regarding Articles 5.10 of the AD Agreement and 11.11 of the SCM Agreement should be resolved in a consistent way.

"the panel shall interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations."

6.16 At the outset, we note that the United States does not rely on the provisions of the SCM Agreement to argue that the standard of review set forth in Article 17.6 of the AD Agreement applies in the present case. We also note that, in light of the Ministerial Decision, the United States does not consider the Article 17.6 standard of review to be of "general application". Rather, the sole basis relied on by the United States for applying the Article 17.6 standard of review is the Ministerial Declaration which, in the opinion of the United States, "must have some meaning".

6.17 We agree that the Ministerial Declaration "must have some meaning". However, it is not immediately apparent from the text of the Ministerial Declaration that it has the meaning attributed to it by the United States.<sup>48</sup> Assuming *arguendo* that it was the intention of the Ministers to introduce the standard of review set forth in Article 17.6 of the AD Agreement into the SCM Agreement (with a view to resolving anti-dumping and countervailing duty disputes in a consistent manner)<sup>49</sup>, there is nothing in the Ministerial Declaration to create any obligations in this regard. We note that the Ministerial Declaration is a mere "Declaration", rather than a "Decision" of the Ministers. In our view, a Declaration lacks the mandatory authority of a Decision. In the Ministerial Declaration, Ministers simply "recognize ... the need" for the consistent resolution of disputes. In our opinion, the simple recognition of the need for an action does not mandate that action. In a Ministerial Decision, by contrast, Ministers "decide" that certain action shall be taken. For these reasons, we do not consider that the Ministerial Declaration imposes any obligations on this Panel. In particular, we do not consider that the Ministerial Declaration requires this Panel to apply the standard of review set forth in Article 17.6 of the AD Agreement.

6.18 We note that, by virtue of Article 30 of the SCM Agreement, the provisions of the DSU are applicable to the settlement of disputes under the SCM Agreement, "except as otherwise specifically provided [t]herein." In the absence of any specific standard of review provided for in the SCM Agreement, we consider that we are subject to the standard of review set forth in Article 11 of the DSU. By virtue of that provision, we are required to "make an objective assessment of the matter before [us], including an objective assessment of ... the applicability of and conformity with the [SCM Agreement]". We note that this approach is entirely consistent with statements made by the Appellate Body in *Hormones*.<sup>50</sup> We also note that the United States has in principle accepted the application of the standard of review set forth in Article 11 of the DSU, in the event that we do not apply the standard of review set forth in Article 17.6 of the AD Agreement.

6.19 The United States has argued that the standard of review provided for in Article 11 of the DSU does not apply in cases "where the agreement at issue is silent with regard to a particular matter even after applying the customary rules of interpretation of public international law." In such cases, the United States argues that panels should apply the same standard of review applied by the GATT panels on *United States Salmon* and *New Zealand Electrical Transformers*. We do not consider it

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<sup>48</sup> Indeed, we note that a further meaning has also been attributed to the Ministerial Declaration by the European Communities.

<sup>49</sup> We note that the matter in the present case is essentially concerned with the existence of a subsidy. This, of course, is not a matter that would ever arise in the context of a dispute concerning anti-dumping duties.

<sup>50</sup> We note in particular that, "[i]n so far as legal questions are concerned - that is, consistency or inconsistency of a Member's measure with the provisions of the applicable agreement - ... Article 11 of the DSU is directly on point, requiring a panel to "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 ..." (*Hormones*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 19 February 1998, para. 118).



necessary to address this argument in any detail, since we disagree with the United States that the SCM Agreement is silent with regard to the particular matter at issue in the present dispute. As explained fully in the next section of our report, we consider Articles 1.1(b), 19.1, 19.4 and 21.1 of the SCM Agreement, and Article VI:3 of the GATT 1994, to be particularly relevant to the matter before us.

C. WERE THE COUNTERVAILING DUTIES IMPOSED AS A RESULT OF THE 1995, 1996 AND 1997 ADMINISTRATIVE REVIEWS CONSISTENT WITH ARTICLES 10 AND 19.4 OF THE SCM AGREEMENT?

6.20 The European Communities claims that the countervailing duties imposed as a result of the administrative reviews initiated in 1995, 1996 and 1997 are inconsistent with Articles 10 and 19.4 of the SCM Agreement because the USDOC failed to take proper account of various changes in ownership concerning the UK leaded bar producers/exporters under review. Since the European Communities' Article 19.4 claim repeats many of the arguments advanced in support of its Article 10 claim, we consider it appropriate to first address the European Communities' Article 10 claim.

6.21 Before examining the substance of the European Communities' Article 10 claim, we shall first review the principal facts surrounding the three administrative reviews at issue.

**1. The Facts**

6.22 From 1967 to 1986, the main UK producer/exporter of hot rolled lead and bismuth carbon steel (hereinafter "leaded bars") was British Steel Corporation ("BSC"). BSC was a state-owned enterprise. United Engineering Steels ("UES") was created in 1986, as a joint venture between BSC and privately-owned Guest, Keen and Nettlefolds ("GKN"). Both BSC and GKN provided assets to UES, in return for equal shares in the joint venture. In particular, BSC spun-off its leaded bar-producing assets (known as the "Special Steels Business") to UES. Negotiations concerning this change in ownership, including the extent of BSC's holding in UES, were conducted at arm's length, consistent with commercial considerations. BSC ceased producing leaded bars after the spin-off of its leaded bar-producing assets to UES.

6.23 BSC was privatized in 1988. As a first step, in September 1988 British Steel public limited company ("BSplc") assumed the property, rights and liabilities of BSC, including BSC's holding in UES. In December 1988, shares in BSplc were sold through the stockmarket. The US Department of Commerce ("USDOC") confirmed that the sale of BSplc shares was at arm's length, for fair market value and consistent with commercial considerations. Henceforth, both UES parent companies (BSplc and GKN) were in private hands. On 20 March 1995 BSplc purchased GKN's holding in UES, whereupon UES was renamed British Steel Engineering Steels ("BSES").

6.24 On 8 May 1992, a countervailing duty investigation was initiated by the United States against imports of leaded bars from, *inter alia*, the United Kingdom. The period of investigation was calendar year 1991. On 27 January 1993, the United States Department of Commerce (USDOC) issued its final determination, but later amended this determination on 12 October 1993 pursuant to a court remand (hereinafter collectively "1993 *Leaded Bars* determination").<sup>51</sup> On 22 March 1993, the USDOC published a countervailing duty order imposing countervailing duties on imports of leaded bars originating *inter alia* in the United Kingdom.<sup>52</sup>

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<sup>51</sup> *Final Affirmative Countervailing Duty Determination: Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 58 Fed. Reg. 6237, and *Remand Determination of US Department of Commerce on General Issues of Privatization, Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 12 October 1993 (unpublished).

<sup>52</sup> 58 Fed. Reg., p. 15327 (hereinafter "1993 *Leaded Bars* duty order").

6.25 In its 1993 *Leaded Bars* determination, the USDOC found that non-recurring,<sup>53</sup> untied<sup>54</sup> subsidies had been bestowed on BSC prior to 1986. The USDOC allocated these subsidies over 15 years, deemed to be the useful life of productive assets in the steel industry.<sup>55</sup> The period over which the pre-1985/86 subsidies were allocated therefore included the creation of UES (1986), the privatization of BSplc (1988), and BSplc's acquisition of UES (1995).

6.26 The USDOC 1993 *Leaded Bars* determination concerned imports of leaded bars produced by UES. The USDOC found that a portion of the pre-1985/86 subsidies provided to BSC "travelled"<sup>56</sup> to UES, via BSC's Special Steels Business. In doing so, the USDOC first calculated the pro rata portion of pre-1985/86 subsidies to BSC (allocated to the period of investigation of the 1993 *Leaded Bars* determination) that could be attributed to its Special Steels Business. Using its "change-in-ownership" methodology, the USDOC then determined what portion of the pre-1985/86 subsidies attributable pro rata to BSC's Special Steels Business during the period of investigation should "pass through" to UES via BSC's Special Steels Business. Countervailing duties were imposed on imports of leaded bars produced by UES on the basis of the portion of benefit "passing through" from BSC to UES during the period of investigation.

6.27 The USDOC's 1993 *Leaded Bars* duty order was subject to administrative review in 1994, 1995, 1996, 1997, 1998 and 1999. The administrative review initiated in 1994<sup>57</sup> covered part of 1992 and all of 1993 imports of leaded bars produced by UES. The administrative review initiated in 1995<sup>58</sup> covered 1994 imports of leaded bars produced by UES. The USDOC applied the methodology described in the preceding paragraph to calculate the amount of countervailing duties to be imposed on such imports.

6.28 The administrative review initiated in 1996<sup>59</sup> covered imports during the calendar year 1995, the year in which BSplc acquired GKN's interest in UES. For 1995 imports of leaded bars prior to BSplc's March 1995 acquisition of UES (*i.e.*, leaded bars produced by UES), the USDOC applied the same "change-in-ownership" methodology as for the 1993 *Leaded Bars* determination, and the 1994 and 1995 administrative reviews.

6.29 For 1995 imports subsequent to BSplc's 20 March 1995 acquisition of UES (*i.e.*, imports of leaded bars produced by BSplc/BSES), the USDOC adopted a two-stage "pass through" approach. First, the USDOC took the benefit of prior BSC subsidies already deemed to have "passed through" to

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<sup>53</sup> The parties do not disagree that these subsidies were "non-recurring". The Panel sees no reason to question the classification of the relevant subsidies as "non-recurring", since they were provided on an irregular basis.

<sup>54</sup> The parties do not disagree that these subsidies were "untied". The Panel sees no reason to question the classification of the relevant subsidies as "untied", since they were provided on a company-wide basis, rather than being directed at specific products.

<sup>55</sup> The Panel understands that the USDOC assumed that the "benefit" from non-recurring, untied "financial contributions" bestowed on BSC would "benefit" BSC's future production, because it would be used for investment in productive assets. It is for this reason that the duration of future "benefit" is determined by reference to the useful life of productive assets in the steel industry. The European Communities has not disputed this approach.

<sup>56</sup> *Remand Determination of US Department of Commerce on General Issues of Privatization, Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 12 October 1993 (unpublished), page 3.

<sup>57</sup> *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 60 Fed. Reg. 44029 (hereinafter "1994 administrative review").

<sup>58</sup> *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 61 Fed. Reg. 58377 (hereinafter "1995 administrative review").

<sup>59</sup> *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 62 Fed. Reg. 53306 (hereinafter "1996 administrative review").

UES (as for pre-20 March 1995 imports), and used its change-in-ownership methodology to allocate that benefit between BSplc (the buyer) and GKN (the seller). Second, the USDOC calculated the benefit "passed through" from BSC to BSplc upon the privatization of BSC.<sup>60</sup> To do so, USDOC calculated all the non-recurring, untied subsidies previously bestowed on BSC, minus those already allocated to UES by virtue of the latter's acquisition of BSC's Special Steels Business assets. This residual category of subsidies to BSC had not been considered by the USDOC before, since BSC had not produced any of the imported leaded bars hitherto taken into account by the USDOC. Using its change-in-ownership methodology, USDOC then allocated a portion of these residual BSC subsidies to BSplc (the buyer of BSC), and a portion to the United Kingdom government (the seller of BSC). Thus, countervailing duties for post-20 March 1995 imports of leaded bars produced by BSplc/BSES were calculated on the basis of (1) "benefit" passing through from UES to BSplc, and (2) "benefit" passing through from BSC to BSplc.

6.30 The administrative review initiated in 1997<sup>61</sup> covered imports during the calendar year 1996. The USDOC adopted the same two-stage approach as in the 1996 administrative review for post-20 March imports of leaded bars produced by BSplc/BSES.

## **2. The EC Article 10 claim**

### **(a) Arguments of the parties**

6.31 We set forth below our understanding of the principal arguments advanced by the parties.

#### *(i) The European Communities*

6.32 The European Communities submits that the three administrative reviews at issue are inconsistent with Article 10 of the SCM Agreement, read in conjunction with Articles 19, 1 and 14 of the SCM Agreement, because they impose countervailing duties on the imports of privately-owned companies without first examining or establishing whether there exists any subsidy relating to those imports. According to the European Communities, Article 10 of the SCM Agreement requires that a WTO Member take "all necessary steps" to ensure that countervailing duties are imposed by its authorities only in conformity with the terms of the SCM Agreement. The European Communities asserts that Article 10 mandates that a Member make a threshold determination of the "existence" of a subsidy before examining other ASCM requirements. Such a determination must occur prior to and wholly distinct from the later determination of the amount of a subsidy, for which it is a necessary condition precedent.

6.33 The European Communities considers that, consistent with the mandate of Article 10, the fundamental requirement first to determine that a "subsidy exists" is also found elsewhere in the SCM Agreement, including Articles 19.1 and 19.4, and in Article VI of the GATT 1994. Article 19.1 establishes that a Member may impose countervailing duties only after making "a final determination of the existence and amount of a subsidy . . .". Article 19.4 ASCM requires that "[n]o countervailing duty shall be levied on any imported product in excess of the amount of the subsidy found to exist . . .". Article VI:3 of the GATT 1994 sets forth the same obligation, requiring that "[n]o countervailing duty shall be levied on any product . . . in excess of an amount equal to . . . the subsidy determined to have been granted. . .".

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<sup>60</sup> Thus, it is only once BSplc acquires full ownership of UES that the privatization of BSC becomes relevant to the USDOC's findings.

<sup>61</sup> *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 63 Fed. Reg. 18369 (hereinafter "1997 administrative review").

6.34 Thus, according to the European Communities, the terms of the SCM Agreement require Members to “take all necessary steps” to demonstrate the existence of a subsidy. Consistent with this plain language, this inquiry must occur before a countervailing measure may be imposed. A Member’s obligation in this regard cannot and does not end with a determination that an unrelated party at some point in the past received a subsidy. According to the European Communities, it must be demonstrated as a result of all available evidence that the party under investigation, whose goods are the ones subject to an offsetting countervailing duty, was the recipient of a subsidy. This means that it must be demonstrated (not arbitrarily assumed) that the party under investigation has either received itself a financial contribution and a benefit, or has benefited from a financial contribution to a third party. By the clear terms of the Agreement, calculating the amount or allocation of a “subsidy” may not take place without first establishing its existence.

6.35 The European Communities notes that, according to Article 1.1 of the SCM Agreement, a “subsidy” exists if a “financial contribution” by a government or public body confers a “benefit”. The European Communities acknowledges that a “financial contribution” was made by the United Kingdom Government to BSC. The European Communities further acknowledges that such financial contributions benefited BSC in the past and constituted “subsidies” to that firm. The European Communities contends, however, that such prior contributions are not “subsidies” in the cases that form the basis for the dispute before this Panel, because they confer no “benefit” on UES or BSplc/BSES, the companies whose products are subject to the relevant US countervailing duty determinations and whose imports into the United States are being assessed for countervailing duties.

6.36 The European Communities submits that, with reference to the context provided by Article 14 of the SCM Agreement, “benefit” must be determined by reference to the market. A “benefit” is only conferred if a “financial contribution” is made available on terms more favourable than those available to the recipient on the market. Accordingly, where a privately-owned company has purchased productive assets at fair market value in an arm’s-length transaction, there can be no benefit conferred on the purchaser within the meaning of the ASCM. A purchaser of formerly state-owned assets at market value is not in any way put in a more advantageous position in comparison to the market.

6.37 The European Communities submits that a “benefit” must be shown to have been conferred on the company whose imports are to be countervailed. According to the European Communities, the record of the *Leaded Bars* determinations before this Panel makes clear that the United States explicitly and repeatedly has refused to enquire as to whether a benefit, and therefore a “subsidy”, was conferred on BSplc/BSES or UES, much less to demonstrate that such a “benefit” was actually conferred. Rather, the United States improperly presumed that such a “benefit” was conferred by stating that a previous contribution to BSC “passed through” to UES and BSplc/BSES without demonstrating the “pass through” as an economic reality or explaining the nature of the “pass through” by reference to the SCM Agreement or to any commercial or market benchmark.

6.38 With reference to footnote 36 to Article 10 of the SCM Agreement, and Article VI.3 of the GATT 1994, the European Communities asserts that the object and purpose of countervailing duties is to offset, or neutralise, a subsidy. A Member may not impose countervailing duties to more than offset a subsidy. The European Communities submits that countervailing duties were levied by the United States on UES and, in turn, BSplc/BSES without any demonstration by the United States of the existence of a “subsidy”. In doing so, the United States by definition imposed countervailing duties that go beyond “offsetting” any subsidy bestowed directly or indirectly upon the manufacture, production or export of subject merchandise by those companies.

(ii) *The United States*

6.39 The United States submits that the USDOC administrative reviews at issue were consistent with Article 10 of the SCM Agreement. According to the United States, the SCM Agreement only directs (in Article 1) that the investigating authority identify the existence of a “subsidy,” including a

subsidy "benefit," as of the time of the subsidy bestowal and (in Article 14) that the investigating authority measure the identified subsidy "benefit" through certain market-rate benchmarks as of the time of the subsidy bestowal.

6.40 In addition, the SCM Agreement contemplates that the measured subsidy "benefit" will be allocated over time, although it does not direct how this allocation must be done. Beyond that, however, the SCM Agreement is silent. It does not address a change in ownership, at least in the context of a countervailing duty proceeding. Specifically, it does not explain whether and, if so, how the investigating authority should take account of a change in ownership taking place after the subsidy bestowal. In fact, the only place where the SCM Agreement addresses changes in ownership is in a provision dealing not with countervailing duty proceedings (under Part V of the SCM Agreement), but rather with WTO subsidy challenges under Part III of the SCM Agreement. That provision, Article 27.13, strongly implies a general rule that previously bestowed subsidies remain actionable and are allocable to the successor company's production following a change in ownership, which is consistent with USDOC's approach but exactly the opposite of the approach advocated by the EC.

6.41 According to the United States, nothing in Article 1 or Article 14 requires the investigating authority to make a new "benefit" determination, or a new measurement of "benefit", simply because the ownership of the original subsidy recipient/beneficiary has changed hands. The United States submits that the SCM Agreement assumes that subsidies satisfying the requirements of Article 1.1 benefit the merchandise produced as a result of those subsidies, regardless of who owns the company or the productive assets used to produce the merchandise and regardless of who purchases the merchandise. In the case of untied, non-recurring subsidies, the relevant financial contribution is deemed to benefit the activities of the subsidized company over a period of time, known as the "benefit stream". Likewise, the United States submits that, because Article 27.13 of the SCM Agreement contemplates a general rule that previously bestowed subsidies remain actionable and are allocable to the production of the surviving privatized company, Article 27.13 implicitly rejects the contrary notion that a subsidy "benefit" must be re-identified or re-measured as of the time of the change in ownership.

6.42 The United States believes that the European Communities is making a crucial -- yet unsupportable -- assumption when it argues that the investigating authority is required to make another "benefit" determination when the ownership of the subsidy recipient changes hands, given that the SCM Agreement requires the investigating authority to establish that the firm under investigation was the subsidy recipient before it may impose duties. The European Communities is assuming that when the ownership of the subsidy recipient changes hands, the successor firm is unrelated to, and different from, the subsidy recipient. Plainly, while the owners may be different and unrelated, the productive assets which benefitted from the subsidy before the change in ownership are the same ones used by the new owners after the change in ownership. The United States argues that the determinative factor is the productive assets -- not the owners -- given that Article VI:3 of the GATT 1994 and Article 10 of the SCM Agreement refer to the "subsidy" as having been "bestowed, directly or indirectly, upon the manufacture, production or export of" the product. In focusing on the productive assets, the United States asserts that the successor firm really is "no different" from the subsidy recipient, and consequently there is no need -- even under the European Communities' theory -- for a second benefit determination after the change in ownership.

6.43 The United States also strongly disagrees with the European Communities' assertion that it is necessary for the investigating authority to demonstrate that the firm under investigation was the actual recipient of the subsidy before it may impose duties. This assertion in no way follows from the fact that the investigating authority must first identify the existence of a subsidy before measuring and allocating the amount of the subsidy found to exist and imposing a countervailing duty. The simple requirement that the investigating authority begin its analysis by first identifying the existence of a subsidy does not shed any light on the question whether the identified benefit must be the one bestowed originally or whether a *continuing* benefit must be identified with regard to the new owner

of the subsidy recipient.<sup>62</sup> Furthermore, the United States considers it especially significant that the European Communities does not, in its view, rely on the text of the provision that directly governs the identification of the subsidy benefit, i.e., Article 1.1(b), or even the context provided by the measurement provisions of Article 14, when it attempts to support its crucial assertion that it is necessary for the investigating authority to demonstrate that the firm under investigation was the subsidy recipient before it may impose duties. Instead, the only support that the EC offers is what it (erroneously) views as the object and purpose of the SCM Agreement, which, according to the EC, is the imposition of duties to offset the continuing subsidy benefit received by the firm under investigation. The United States concedes that, in the context of the SCM Agreement, there must be, as a practical matter, some entity or individual that receives the Article 1.1 financial contribution. However, this by itself does not mean that the Article 1.1 "benefit" is to that recipient entity or individual. In fact, Article 1.1 itself is silent regarding who or what is the beneficiary of a subsidy. Article VI:3 of GATT 1994 and Article 10 of the SCM Agreement, meanwhile, provide that the purpose of imposing countervailing duties is to offset subsidies bestowed on the manufacture, production or export of the merchandise. In other words, the United States submits that these provisions contemplate that a subsidy benefits the manufacture, production or export of merchandise.

6.44 The United States asserts that the USDOC's change-in-ownership methodology is consistent with the object and purpose of the SCM Agreement, which is to deter and offset trade-distorting government subsidies benefitting merchandise and causing injury to an industry in an importing country. Consistent with this object and purpose, USDOC's methodology helps to remedy the injurious trade distortions that result from government subsidization even after the ownership of the subsidy recipient/beneficiary has changed hands in an arm's length, fair market value transaction. In the United States' view, the European Communities has misstated the object and purpose of the SCM Agreement as being the imposition of duties to offset the continuing subsidy benefit received by the firm under investigation. The United States asserts that the object and purpose of the SCM Agreement is, in fact, to deter and offset trade-distorting government subsidies benefitting merchandise and causing injury to an industry in the importing country. The United States submits that the USDOC imposes countervailing duties in a change-in-ownership situation in order to offset the subsidization found to exist, just as is contemplated by Article 19.4 of the SCM Agreement. The United States does not impose any additional duties in an effort to deter subsidization.

(b) Evaluation by the Panel

6.45 Article 10 of the SCM Agreement provides in relevant 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." (\* footnote omitted)

6.46 In applying Article 10 of the SCM Agreement, we recall that Article 3.2 of the DSU requires panels to interpret "covered agreements", including the SCM Agreement, "in accordance with customary rules of interpretation of public international law". The rules of treaty interpretation set forth in Article 31 of the Vienna Convention on the Law of Treaties ("Vienna Convention"), have

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<sup>62</sup> The United States agrees that the investigating authority must first identify the existence of a subsidy, i.e., a "financial contribution" and a "benefit," before measuring and allocating the amount of the subsidy found to exist or imposing a countervailing duty. The United States notes, however, that when the investigating authority uses the benefit-to-recipient measurement standard, the act of identifying the benefit (under Article 1 of the SCM Agreement) is normally the same as measuring the benefit (under Article 14 of the SCM Agreement). The separate act of allocating the identified and measured benefit over time can only be done afterwards.

"attained the status of a rule of customary or general international law".<sup>63</sup> Article 31.1 of the Vienna Convention provides:

"A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose".

6.47 By virtue of the ordinary meaning of Article 10, a Member is required to "take all necessary steps" to ensure that any countervailing duty it applies is "in accordance with" Article VI of GATT 1994 and the terms of the SCM Agreement. A Member will therefore violate Article 10 if it imposes a countervailing duty that is not "in accordance with" Article VI of GATT 1994 or the terms of the SCM Agreement.

(ii) *Conditions for the imposition of countervailing duties*

6.48 The European Communities has argued that the United States has violated Article 10 by imposing countervailing duties on imports of leaded bars produced by UES and BSplc/BSES in a manner not in accordance with Article 19 of the SCM Agreement or Article VI:3 of the GATT 1994. According to the European Communities, paragraphs 1 and 4 of Article 19 of the SCM Agreement require the United States to demonstrate the existence of a subsidy in respect of imports of leaded bars produced by UES and BSplc/BSES before imposing countervailing duties on such imports.

6.49 Article 19.1 of the SCM Agreement provides:

"If, after reasonable efforts have been made to complete consultations, a Member makes a final determination of the existence and amount of the subsidy and that, through the effects of the subsidy, the subsidized imports are causing injury, it may impose a countervailing duty in accordance with the provisions of this Article unless the subsidy or subsidies are withdrawn."

6.50 Consistent with the ordinary meaning of Article 19.1, the imposition by a Member of a countervailing duty on an imported product is subject to two conditions. First, the Member must have made a final determination of the existence and amount of a (countervailable)<sup>64</sup> subsidy in respect of the imported products. Second, the Member must have made a final determination that the subsidized imports are causing injury to the relevant domestic industry. Leaving aside the issue of injury, Article 19.1 is therefore clearly based on the premise that no countervailing duties shall be imposed on imported products unless the existence (and amount) of a (countervailable) subsidy is demonstrated in respect of such imports.

6.51 Article 19.4 of the SCM Agreement provides that:

"No countervailing duty shall be levied\* on any imported product in excess of the amount of the subsidy found to exist, calculated in terms of subsidization per unit of the subsidized and exported product." (\* footnote omitted)

6.52 By virtue of the ordinary meaning of the text of Article 19.4 of the SCM Agreement, any countervailing duty imposed on an imported product shall not exceed the amount of subsidy found to exist in respect of the imported product. Logically, and consistent with the ordinary meaning of Article 19.4, no countervailing duty may be imposed on an imported product if no (countervailable)

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<sup>63</sup> *United States - Standards for Reformulated and Conventional Gasoline* (hereinafter "*Gasoline*"), WT/DS2/AB/R, adopted 20 May 1996, p. 17.

<sup>64</sup> A subsidy is "countervailable" when it is (1) specific within the meaning of Article 2 of the SCM Agreement, and (2) not non-actionable by virtue of Part IV of the SCM Agreement.

subsidy is found to exist with respect to that imported product, since in such cases the amount of subsidy found to exist with respect to the imported product would be zero. Thus, like Article 19.1, Article 19.4 of the SCM Agreement establishes a clear nexus between the imposition of a countervailing duty, and the existence of a (countervailable) subsidy.

6.53 The same nexus between the imposition of a countervailing duty and the existence of a (countervailable) subsidy underlies Article VI:3 of the GATT 1994, which provides in relevant part:

"No countervailing duty shall be levied on any product of the territory of any contracting party imported into the territory of another contracting party in excess of the amount equal to the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product in the country of origin or exportation, including any special subsidy to the transportation of a particular period."

6.54 We believe that at least one other provision of the SCM Agreement is equally relevant in the present context, since it is also based on the premise that no countervailing duties shall be imposed absent (countervailable) subsidization. That provision is Article 21.1, which provides that:

"A countervailing duty shall remain in force only as long as and to the extent necessary to counteract subsidization which is causing injury."

6.55 By virtue of Article 21.1, countervailing duties may only remain in force so long as there is (1) (countervailable) subsidization, and (2) injury caused by such subsidization. Thus, Article 21.1 establishes a clear link between the (continued) imposition of countervailing duties and the (continued) existence of (countervailable) subsidization.

6.56 In our view, the above provisions are all based on the premise that no countervailing duty may be imposed absent (countervailable) subsidization. Furthermore, we consider that this premise underlies the very purpose of the countervailing measures envisaged by Part V of the SCM Agreement. Footnote 36 to Article 10 of the SCM Agreement provides that "[t]he 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" (emphasis supplied). Thus, the imposition of a countervailing duty is only envisaged in circumstances where it is necessary to "offset" a (countervailable) subsidy. In our view, footnote 36 to Article 10 does not envisage the imposition of countervailing duties when no (countervailable) subsidy is found to exist, for in such cases there would be no (countervailable) subsidy to "offset". We note that the parties agree with our understanding of the object and purpose of the countervailing measures envisaged by Part V of the SCM Agreement. The European Communities has stated that "the established purpose for assessment of countervailing duties is to offset the advantage afforded imported merchandise by a subsidy bestowed upon the manufacture, production or export of that merchandise."<sup>65</sup> Despite a different understanding of the object and purpose of the SCM Agreement more generally, the United States has confirmed that the "USDOC imposes countervailing duties in a change-in-ownership situation in order to *offset* the subsidization found to exist, just as is contemplated by Article 19.4 of the SCM Agreement."<sup>66</sup>

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<sup>65</sup> See Attachment 1.1, para. 95.

<sup>66</sup> See Attachment 2.6, para. 80. Initially, the United States was understood by the European Communities to argue that countervailing duties were intended to deter subsidization. At the aforementioned paragraph of the aforementioned submission, the United States clarified that this was not the case: "[t]he United States does not impose any additional duties in an effort to *deter* subsidization. That being said, the United States remains of the view that the mere existence of the disciplines found in the SCM Agreement inherently deters governments from subsidizing, and deterrence is indeed one of the purposes of the SCM Agreement."



6.57 Thus, consistent with the fundamental premise underlying Articles 19.1, 19.4, and 21.1 of the SCM Agreement, and Article VI:3 of the GATT 1994, and consistent with the object and purpose of countervailing duties envisaged by Part V of the SCM Agreement, we consider that a countervailing duty may only be imposed on an imported product if it is demonstrated that a (countervailable) subsidy was bestowed directly or indirectly on the manufacture, production or export<sup>67</sup> of that merchandise.<sup>68</sup> Since the United States imposed countervailing duties on 1994, 1995 and 1996 imports of leaded bars, we consider that, in light of the fundamental premise underlying Articles 19.1, 19.4, and 21.1 of the SCM Agreement, Article VI:3 of the GATT 1994, and the object and purpose of countervailing duties, the United States was effectively required, by virtue of Article 10, to demonstrate that a (countervailable) subsidy was bestowed directly or indirectly on the production of those imports. In order to determine whether the United States satisfied this requirement, it is necessary to examine the criteria for determining the existence of a "subsidy".

(iii) *The existence of "benefit"*

6.58 The criteria for determining the existence of a subsidy are set forth in Article 1 of the SCM Agreement. In short, Article 1.1 of the SCM Agreement provides that a subsidy exists if a "financial contribution" by a government or public body confers a "benefit". In challenging the USDOC findings that subsidies were bestowed on the production of leaded bars produced by UES and BSpIc, the European Communities asserts that the "financial contributions" to BSC did not confer any "benefit" on UES or BSpIc. It is the alleged absence of any finding of "benefit" to UES or BSpIc which forms the basis for the European Communities' Article 10 claim.<sup>69</sup>

6.59 With regard to the existence of "benefit", the United States has informed us that:

"the U.S. countervailing duty statute contains 'the irrebuttable presumption that nonrecurring subsidies benefit merchandise produced by the recipient over time,' without requiring any re-evaluation of those subsidies based on the use or effect of those subsidies or subsequent events in the marketplace.

The 'irrebuttable presumption' concept, as used in this context, is simply a reference to USDOC's normal allocation methodology. Under that methodology, which applies to so-called 'non-recurring' subsidies, (footnote omitted) USDOC allocates the measured subsidy benefit over time, i.e., to future production, pursuant to a standard declining balance formula that generates a net present value equal to the amount of the subsidy. The period of time selected for this allocation is based on the subsidy

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Without taking any position on the alleged deterrent effect of the existence of the disciplines found in the SCM Agreement, we agree with the United States that countervailing duties should not be imposed in order to deter subsidization.

<sup>67</sup> As the present case concerns alleged production subsidies, we shall give no further consideration to the potential existence of subsidies bestowed directly or indirectly on manufacture or export.

<sup>68</sup> The United States appears to accept the premise that a countervailing duty may only be imposed if there is subsidization. In its first submission, the United States asserted that the USDOC "is authorized to impose duties on the showing that two statutory requirements are satisfied: "(1) **a subsidy is provided with respect to the manufacture, production, or sale of a class or kind of merchandise**; and (2) a domestic industry is injured by reason of imports into the United States of that class or kind of merchandise." (See Attachment 2.1, para. 58 (emphasis supplied).

<sup>69</sup> The European Communities is not disputing the existence of relevant "financial contributions". We agree fully with the European Communities in this regard, since a "financial contribution" does not have to be bestowed directly on a company in order to confer a "benefit" on that company. For example, one company may be found to "benefit" from a "financial contribution" conferred on another company. Furthermore, in certain circumstances an untied, non-recurring "financial contribution" bestowed directly on, and benefiting, a prior company may be deemed to have been bestowed indirectly on the successor company.

recipient's average useful life of assets. ... On the basis of these principles, USDOC affirmatively adopted the approach of treating non-recurring subsidies previously provided to the seller as potentially allocable to the production transferred to the purchaser in a privatization or other change-in-ownership transaction, such as when a government-owned company sells one of its productive units."<sup>70</sup>

6.60 This approach was explained further by the USDOC in its 1993 *Leaded Bars* determination, where the USDOC examined whether "potentially allocable subsidies ... could have travelled with the productive unit" following a change in ownership.<sup>71</sup>

6.61 In its 1993 *Leaded Bars* determination, the USDOC "calculate[d] the benefit from prior subsidies which passed through from BSC to UES"<sup>72</sup> when UES acquired BSC's Special Steels Business, the latter considered by the USDOC to be a "productive unit." The USDOC explained that "[w]hen a productive unit is sold by a company which continues to operate (such as BSC), the potentially allocable subsidies which could have travelled with the productive unit, but did not because they were accounted for as part of the purchase price, simply stay with the selling company. As such, they have not been extinguished. Instead, they continue to benefit the seller and our calculation represents the allocation of the subsidies between the seller and the productive unit it has sold." As a result, the USDOC imposed countervailing duties on imports of leaded bars produced by UES, based on that portion of "benefit" from prior subsidies that was deemed by the USDOC to have passed through to UES. With regard to the existence of "benefit" in particular, we understand the USDOC to have found that "benefit" conferred on BSC by pre-1985/86 "financial contributions" to BSC passed through in part to UES. This understanding is confirmed by the USDOC in its 1995 administrative review of its 1993 *Leaded Bars* duty order, in which it stated that "when UES was formed, a portion of the pre-1985/86 subsidies provided to BSC continued to benefit the production of UES."<sup>36</sup>

6.62 In its 1995 administrative review, the USDOC "found that UES continues to benefit from subsidies received by BSC",<sup>73</sup> and continued to impose countervailing duties on 1994 imports of leaded bars produced by UES. The USDOC effectively made the same finding of "benefit" with respect to UES in its 1996 administrative review, and therefore continued to impose countervailing duties on 1995 imports of leaded bars produced by UES. In its 1996 administrative review, the USDOC also found that a portion of pre-1985/86 subsidies bestowed on BSC "travel[ed]" to BSplc/BSES.<sup>74</sup> Again, with regard to the existence of "benefit" in particular, we understand the USDOC to have found that the "benefit" conferred on BSC by pre-1985/86 "financial contributions" to BSC passed through to BSplc/BSES. As a result, the USDOC imposed countervailing duties on 1995 imports of leaded bars produced by BSplc/BSES. The USDOC effectively made the same

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<sup>70</sup> See Attachment 2.1, paras. 43, 44 and 46.

<sup>71</sup> *Remand Determination of US Department of Commerce on General Issues of Privatization, Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 12 October 1993 (unpublished), page 5. We note that at page 6240 of its 27 January 1993 determination, the USDOC stated that "as [a subsidized] company disposes of its productive entities, these entities take a portion of the [subsidy] benefits with them when they 'travel to their new home'."

<sup>72</sup> *Remand Determination of US Department of Commerce on General Issues of Privatization, Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*, 12 October 1993 (unpublished), page 2.

<sup>73</sup> *Ibid.*

<sup>74</sup> 1996 administrative review, at p. 53308.

finding of "benefit" with respect to BSplc/BSES in its 1997 administrative review, and continued to impose countervailing duties on 1996 imports of leaded bars produced by BSplc/BSES.<sup>75</sup>

6.63 Are the USDOC's findings on "benefit" sufficient to determine that subsidies were bestowed on the production by UES and BSplc/BSES respectively of leaded bars imported into the United States in 1994, 1995 and 1996? In our view, a proper interpretation of the term "benefit" provides the key for resolving this issue.

6.64 The term "benefit" was recently interpreted by the *Canada Aircraft* panel. That panel found that:

"... the ordinary meaning of 'benefit' clearly encompasses some form of advantage. ... In order to determine whether a financial contribution (in the sense of Article 1.1(a)(i)) confers a 'benefit', i.e., an advantage, it is necessary to determine whether the financial contribution places the recipient in a more advantageous position than would have been the case but for the financial contribution. In our view, the only logical basis for determining the position the recipient would have been in absent the financial contribution is the market. Accordingly, a financial contribution will only confer a 'benefit', i.e., an advantage, if it is provided on terms that are more advantageous than those that would have been available to the recipient on the market."<sup>76</sup>

6.65 The *Canada Aircraft* panel's interpretation of "benefit" was upheld by the Appellate Body. The Appellate Body stated that:

"A 'benefit' does not exist in the abstract, but must be received and enjoyed by a beneficiary or a recipient. Logically, a 'benefit' can be said to arise only if a person, natural or legal, or a group of persons, has in fact received something. The term 'benefit', therefore, implies that there must be a recipient."

"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."<sup>77</sup>

6.66 We agree with the approach of the panel and the Appellate Body in *Canada Aircraft*.<sup>78</sup> In our view, the existence or non-existence of "benefit" rests on whether the potential recipient or beneficiary, which "logically" must be a legal or natural person, or group of persons, has received a 'financial contribution' on terms more favourable than those available to the potential recipient or beneficiary in the market. Moreover, in the particular context of countervailing duties, we believe

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<sup>75</sup> We note that the USDOC recently completed its 1998 administrative review of the 1993 *Leaded Bars* duty order (64 Fed. Reg., Number 154). The 1999 administrative review of the 1993 *Leaded Bars* duty order was initiated on 30 April 1999 (64 Fed. Reg., at p. 23269).

<sup>76</sup> *Canada Aircraft*, WT/DS70/R, adopted 20 August 1999, para. 9.112.

<sup>77</sup> *Canada Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, paras. 154 and 157.

<sup>78</sup> We recall that, while adopted panel reports are not binding on subsequent panels, they do create "legitimate expectations among WTO Members, and therefore, should be taken into account where they are relevant to any dispute" (*Japan - Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, 4 October 1996, p. 14). We consider the same to be true of adopted Appellate Body reports.

that consideration should also be given to Article VI:3 of the GATT 1994, and footnote 36 to Article 10 of the SCM Agreement.

6.67 Article VI:3 of the GATT 1994 provides in relevant part:

"The term 'countervailing duty' shall be understood to mean a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export of any merchandise."

6.68 Footnote 36 to Article 10 of the SCM Agreement provides that:

"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."

6.69 These provisions state that countervailing duties levied on imported products are intended to offset (countervailable) subsidies found to have been bestowed on *inter alia* the production of such imported products. The notion of "subsidy" comprises two elements: (1) "financial contribution, and (2) "benefit". As noted above, "benefit" is determined by reference to the terms on which a "financial contribution" would have been made available to a particular legal or natural person, or group of persons, in the market. Full consideration of Article VI:3 of the GATT 1994 and footnote 36 to Article 10 of the SCM Agreement leads us to conclude that, in the context of countervailing duty investigations, the existence of a "benefit" should be determined by reference to the market terms on which a "financial contribution" bestowed directly or indirectly upon the production of any merchandise would have been made available to the producer of that merchandise. Thus, in order to determine whether any subsidy was bestowed on the production by UES and BSplc/BSES respectively of leaded bars imported into the United States in 1994, 1995 and 1996, it is necessary to determine whether there was any "benefit" to UES and BSplc respectively (*i.e.*, the producers of the imported leaded bars at issue).

6.70 We recall the US argument that the USDOC was not required to find "benefit" to UES and BSplc/BSES specifically, because BSC, UES and BSplc/BSES are not "different companies", since the operations of UES and BSplc are "essentially the same as"<sup>79</sup> the operations of BSC. We, however, are in no doubt that, for the purpose of determining "benefit", a clear distinction should be drawn between BSC, and UES and BSplc/BSES respectively. This is because the changes in ownership leading to the creation of UES and BSplc/BSES involved the payment of consideration for the productive assets etc. acquired by those entities from BSC. Since the finding of "benefit" to BSC was effectively based on BSC acquiring those productive assets etc. for free,<sup>80</sup> the fact that consideration is provided for those productive assets etc. by UES and BSplc/BSES, or the owners thereof, must raise the possibility that the original "benefit" determination in respect of BSC is no longer valid<sup>81</sup> for UES and BSplc/BSES respectively. For this reason, we consider that the changes in ownership leading to the creation of UES and BSplc/BSES should have caused the USDOC to examine whether the

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<sup>79</sup> See Attachment 2.8, para. 3.

<sup>80</sup> The term "benefit" effectively represents the portion of a "financial contribution" that, by reference to a market benchmark, the recipient gets for "free". This is the portion of a "financial contribution" that, by reference to a market benchmark, the recipient has not "paid for". In the case of "benefit" conferred by untied, non-recurring "financial contributions", the United States presumes that such "benefit" is used to benefit future production through investment in productive assets. In this sense, the beneficiary of untied, non-recurring "financial contributions" is deemed to have acquired productive assets for "free". The European Communities has not disputed this approach in respect of "benefit" to BSC.

<sup>81</sup> The original "benefit" determination may not remain valid either because there is no longer any "benefit" conferred on the successor company, or because the amount of "benefit" conferred on the successor company is less than that conferred on the prior company.

production of leaded bars by UES and BSplc/BSES respectively, and not BSC, was subsidized. In particular, the USDOC should have examined the continued existence of "benefit" already deemed to have been conferred by the pre-1985/86 "financial contributions" to BSC, and it should have done so from the perspective of UES and BSplc/BSES respectively, and not BSC.

6.71 The United States has argued that there is no need to determine "benefit" in respect of successor companies, because there is an "irrebuttable presumption" that "benefit" continues to flow from untied, non-recurring "financial contributions", even after changes in ownership. The European Communities has argued that any such presumption can never be "irrebuttable". We agree with the European Communities in this regard. We consider that the presumption of "benefit" flowing from untied, non-recurring "financial contributions" is rebutted in the circumstances surrounding the changes in ownership leading to the creation of UES and BSplc/BSES respectively. In such circumstances, the continued existence of "benefit" to UES and BSplc/BSES respectively must be demonstrated.

6.72 This conclusion, which is founded on a proper interpretation of Article 1.1(b) of the ASCM, is necessarily at odds with the US argument that Article 1.1(b) of the ASCM only requires "benefit" to be established once, as of the time of bestowal of the "financial contribution". The United States based that argument on the fact that Article 1.1 describes the relevant "financial contribution" and "benefit" in the present tense. According to the United States, "the ordinary meaning arising from the use of the present tense to describe both elements is that Article 1.1 is concerned with, and requires the identification of, the 'benefit' that is conferred at the time that the government provides the 'financial contribution'". The United States supports its interpretation of Article 1.1. by reference to the four examples of "financial contributions" contained in Article 14. According to the United States, "[if] there is a general rule that can be derived from the text of Article 14, it is that the investigating authority should look to the time of the subsidy bestowal for the measurement of the subsidy benefit". On the basis of these interpretations of Articles 1.1 and 14, the United States concludes that "the SCM Agreement assumes that subsidies satisfying the requirements of Article 1.1 benefit the merchandise produced as a result of those subsidies, regardless of who owns the company or the productive assets used to produce the merchandise and regardless of who purchases the merchandise".<sup>82</sup>

6.73 We are not convinced by the US interpretation of the use of the present tense in Article 1.1 of the SCM Agreement. In our view, the use of the present tense simply means that the requisite "financial contribution" and "benefit" must exist during the relevant period of investigation or review. The use of the present tense does not speak to the issue of whether or not the existence of "benefit" should be determined at the time of bestowal of the "financial contribution", or whether or not there is any need for any subsequent review of the original determination of "financial contribution" and / or "benefit".<sup>83</sup> It simply means that when an investigation or review takes place, the investigating authority must establish the existence of a "financial contribution" and "benefit" during the relevant period of investigation or review. Only then will that investigating authority be able to conclude, to the satisfaction of Article 1.1 (and Article 21), that there **is** a "financial contribution", and that a "benefit" **is** thereby conferred.

6.74 In respect of Article 14 of the SCM Agreement, the United States asserts that "benefit" should be determined by reference to the market practice prevailing **at the time that** each of the four types of "financial contribution" identified in that provision is bestowed. We do not share the United States' temporal interpretation of Article 14. Certainly, this interpretation is not consistent with the ordinary meaning of the text of that provision. Nothing in the text of Article 14 restricts the analysis envisaged in sub-paragraphs (a) – (d) of that provision to the time at which the relevant "financial contribution"

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<sup>82</sup> See Attachment 2.1, para. 133.

<sup>83</sup> The need for a review is determined by provisions such as Article 21.1, 21.2 and 21.3 of the SCM Agreement.

was bestowed. In our view, Article 14 simply does what it says it does: it provides guidelines to be respected by Members whenever they calculate "benefit". Those guidelines apply whether "benefit" is calculated at the time of bestowal, or at some subsequent time. Article 14 does not, therefore, guide Members as to when that calculation of "benefit" should take place.

6.75 The United States has also relied heavily on Article 27.13 of the SCM Agreement to reject the notion that a subsidy "benefit" must be re-identified or re-measured at some time subsequent to the initial bestowal of the relevant "financial contribution". The basis for the US argument is that Article 27.13 "contemplates a general rule that previously bestowed subsidies remain actionable and are allocable to the production of the surviving privatized company".<sup>84</sup>

6.76 We note that the scope of Article 27.13 is restricted to the application of Part III of the SCM Agreement vis-à-vis certain subsidies "granted within and directly linked to a privatization programme of a developing country Member". Given that the scope of Article 27.13 is construed in such narrow terms, we hesitate before relying on that provision as context to draw conclusions regarding the conferral of "benefit" by "financial contributions"<sup>85</sup> that, as in this case, were manifestly not "granted within and directly linked to" privatization programmes of a developing Member.<sup>86</sup> We are particularly hesitant given that the conclusion we are asked to draw – namely that there is no requirement under Part V of the SCM Agreement for "benefit" to be re-identified or re-measured at some time subsequent to the initial bestowal of the "financial contribution" -- is contrary to what we consider to be the proper interpretation of the term "benefit". In any event, we note that our interpretation of "benefit" would not necessarily render pre-change in ownership "financial contributions" non-actionable: it simply means that, with regard to certain changes in ownership, pre-change in ownership "financial contributions" will only remain actionable if a valid, post-change in ownership, "benefit" determination has been made.<sup>87</sup>

6.77 In order to further explain why it was not necessary for the USDOC to revisit its original "benefit" determination, the United States argued that a determination of "benefit" is not specific to a particular legal or natural person, so that there was therefore no obligation on the USDOC to find "benefit" to UES and BSplc/BSES specifically. According to the United States, "in the context of the SCM Agreement, there must be, as a practical matter, some entity or individual that receives the Article 1.1 financial contribution. However, this by itself does not mean that the Article 1.1 "benefit" is to that recipient entity or individual. In fact, Article 1.1 itself is silent regarding who or what is the beneficiary of a subsidy. Article VI:3 of GATT 1994 and Article 10 of the SCM Agreement ... provide that the purpose of imposing countervailing duties is to offset subsidies bestowed on the manufacture, production or export of the merchandise. In other words, these provisions contemplate that a subsidy benefits the manufacture, production or export of merchandise."<sup>88</sup>

6.78 In light of our interpretation of the term "benefit", and with reference to the statement by the Appellate Body that "[a] 'benefit' does not exist in the abstract, but must be received and enjoyed by a beneficiary or a recipient", we disagree that "benefit" is conferred on the manufacture, production or export of merchandise, irrespective and without consideration of the person(s) manufacturing,

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<sup>84</sup> See Attachment 2.1, para. 156.

<sup>85</sup> We also agree with the European Communities that Article 27.13 pre-supposes the existence of a "subsidy", and would therefore provide little guidance in the context of determining whether or not a "subsidy" or, more particularly, a "benefit", actually exists.

<sup>86</sup> The United States asks the Panel to conclude that Article 27.13 refers to pre-privatization subsidies (See Attachment 2.5, para. 61). To the extent that a pre-privatization subsidy is "granted within and directly linked to" a privatization programme of a developing country Member, we would agree with the United States. However, consistent with the ordinary meaning of the text of Article 27.13, pre-privatization subsidies that are not "granted within and directly linked to" a privatization programme, such as in this case, would clearly fall outside the scope of that provision.

<sup>87</sup> See para. 6.81 below.

<sup>88</sup> See Attachment 2.8, para. 43.

producing, or exporting, the product. In particular, we disagree with the US assertion that "Article 1.1 itself is silent regarding who or what is the beneficiary of a subsidy."<sup>89</sup> In our view, the US approach to determining "benefit" would be abstract in the extreme, since it is impossible to determine whether any "financial contribution" bestowed on manufacture, production or export *per se* is or was made on terms more favourable than those which manufacture, production or export *per se* could have obtained in the market.<sup>90</sup>

6.79 Thus, we are not convinced by the US arguments that, following the relevant changes in ownership, it was not incumbent on the USDOC to demonstrate the continued existence of "benefit" from the perspective of UES and BSplc/BSES, subsequent to the time of bestowal of the relevant "financial contributions".

(iv) *"Benefit" to UES and BSplc/BSES*

6.80 Consistent with the proper interpretation of the term "benefit", any finding of "benefit" to UES or BSplc/BSES, the producers at issue, must be based on market criteria. In particular, it is necessary to determine whether any "financial contribution" was bestowed on UES or BSplc/BSES on terms more favourable than UES or BSplc/BSES respectively could have obtained in the market.

6.81 We recall that BSC's leaded bar assets were spun-off to UES in 1986. The USDOC found that the transaction "represented an arm's length transaction in which BSC acted consistently with commercial considerations".<sup>91</sup> The United States has not denied that the BSC spin-off was negotiated for fair market value. Furthermore, we recall that BSplc was fully privatized in December 1988. The USDOC found that the privatization of BSplc "was at arm's length, for fair market value and consistent with commercial considerations."<sup>92</sup> Thus, fair market value was paid for all productive assets, goodwill etc. employed by UES and BSplc/BSES in the production of leaded bars imported into the United States in 1994, 1995 and 1996. In these circumstances, we fail to see how pre-1985/86 "financial contributions" bestowed on BSC could subsequently be considered to confer a "benefit" on UES and BSplc/BSES during the relevant periods of review.<sup>93</sup> This does not mean that the pre-1985/86 "financial contributions" bestowed on BSC are necessarily irrelevant for the purpose of determining subsidization of the production of leaded bars by UES and BSplc/BSES. As noted above,<sup>94</sup> we consider that an untied, non-recurring "financial contribution" bestowed on a prior company may constitute a "financial contribution" bestowed indirectly on a successor company. This is because the untied, non-recurring "financial contribution" will be deemed to have been invested in the productive assets etc. of that company. Thus, when those productive assets etc. are acquired by the successor company, the successor company indirectly acquires the "financial contribution" embodied in those productive assets etc. Assuming "financial contributions" bestowed directly on

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<sup>89</sup> See Attachment 2.8, para. 43.

<sup>90</sup> In the case of equity infusions, for example, the existence of "benefit" is normally determined by reference to the equityworthiness of the firm into which the capital is injected. A "benefit" will be conferred if that firm is not equityworthy. A similar approach would not be possible if "benefit" were determined from the perspective of the firm's manufacture, production, or export *per se*, since it would obviously be impossible to determine the equityworthiness of the firm's manufacture, production, or export, *per se*.

<sup>91</sup> 1993 *Leaded Bars* determination, at p. 6244.

<sup>92</sup> *Remand Determination of US Department of Commerce on General Issues of Privatization, Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom, 12 October 1993 (unpublished)*.

<sup>93</sup> In *Stainless Steel Sheet and Strip in Coils from France*, the USDOC investigated whether the sale of assets to a government constituted a countervailable subsidy. The USDOC "found no evidence to indicate that the transaction was anything other than an arms-length (*sic*) transaction for full market value. Accordingly, [the USDOC] determine[d] that this program does not constitute a countervailable subsidy ..." Although the investigation of that transaction did not concern the application of the USDOC's change-in-ownership methodology, we nevertheless find it instructive that the USDOC found that the sale of assets did not constitute a subsidy precisely because the sale was an arm's length transaction for full market value.

<sup>94</sup> See note 69 above.

BSC could be deemed to have been bestowed indirectly on UES and BSplc/BSES, this fact alone would not mean that pre-1985/86, untied, non-recurring "financial contributions" bestowed on BSC necessarily confer any "benefit" on UES or BSplc/BSES. This would only be the case if those "financial contributions" were found to have been bestowed indirectly (*i.e.*, through the relevant change-in-ownership transactions) on UES and BSplc/BSES respectively on terms more favourable than UES and BSplc/BSES respectively could have obtained in the market. We consider that such a finding would only be possible if fair market value was not paid for all productive assets etc. acquired by UES and BSplc/BSES respectively from BSC. Since fair market value was paid for all such productive assets etc., we do not consider that any untied, non-recurring "financial contribution" bestowed indirectly on UES and BSplc/BSES could be deemed to confer a "benefit" on those entities.<sup>95</sup>

6.82 In our view, it is irrelevant that the aforementioned fair market value was paid by the (new) owners of UES and BSplc/BSES respectively, rather than those companies themselves. Any approach requiring that fair market value be paid by the company itself, rather than its owners, would elevate form over substance. In the context of privatizations negotiated at arm's length, for fair market value, and consistent with commercial principles, the distinction between a company and its owners is redundant for the purpose of establishing "benefit". Following privatization at arm's length, for fair market value, and consistent with commercial principles, the owners of the privatized company will be profit-maximizers, set on obtaining a market return on the entirety of their investment in the privatized company. Ultimately, therefore, the owners' investment in the privatized company will be recouped through the privatized company providing its owners a market return on the full amount of their investment. In such circumstances, it would be misleading in the extreme to suggest that the price paid by the owners of the privatized company is not ultimately paid by the privatized company itself.

6.83 We note that the USDOC adopted a similar approach to the distinction between a company and its owners in the context of privatization. In 1993, certain petitioners argued before the USDOC that a subsidy should only be considered repaid in the context of privatization if the monies paid to the government -- in the form of the purchase price paid for the privatized company -- came from that company's own funds, and not those of the new owners of that company. The USDOC rejected that argument in the following terms:

"Merely because a company has been incorporated to protect its owners from the company's legal liabilities or for beneficial tax and accounting purposes (or both), it does not follow that the financial condition of the owners is irrelevant to the financial position of the firm. The form in which new owners purchase the government company creates no appreciable difference in how that company will be operated overall. The fact that the owners are shareholders and raise capital to purchase the government-owned company through new share issuings, rather than the company itself taking on debt, does not mean that the owners can be indifferent to the profit margin the company generates, as petitioners assert.

Rather, in the real-world marketplace, the owner-shareholders' expectations of a return on their investment cannot be separated from the profitability of the newly

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<sup>95</sup> We note the US reference to "injurious trade distortions that result from government subsidization even after the ownership of the subsidy recipient/beneficiary has changed hands in an arm's length, fair market value transaction" (See Attachment 2.1, para. 150). We do not need to take any position on whether or not any such "injurious trade distortions" persist after a fair market value change-in-ownership negotiated at arm's length, since the existence of "injurious trade distortions" is not relevant to a proper determination of the existence of "benefit" within the meaning of Article 1.1(b) of the SCM Agreement. The existence of "benefit" is determined simply by reference to the terms on which a "financial contribution" could be obtained by the recipient on the market.



privatized company. Privatized companies (and their assets) are now owned and controlled by private parties who are profit-maximizers. Unlike the former company, which did not need to earn a return on capital when owned and controlled by the government (i.e., when the government is 100 percent owner there is no necessity of paying dividends to itself), the privatized firm now faces the same capital market as its competitors. ... Put another way, the privatized company now has an obligation to provide to its private owners a market return on the company's full value. The owners will seek to extract a rate of return from their company at least equal to that of alternative investments of similar risk. There is, then, no appreciable difference, as reflected in the marketplace, between the profit-making ability of the company and the owners' realization of a profitable return on their investment in that firm.

To adopt the petitioners' rationale that only a full repayment by the new company can extinguish past subsidies would create a test that would elevate form over substance and produce incentives for foreign governments merely to alter the form of the privatization to satisfy this artificial distinction. If the Department were to ratify such a test, owners could simply lend the company the money to repay at least some portion of the past subsidies, taking the capital out as loan payments, rather than dividends. ... Therefore, a private party purchasing all or part of a government-owned company (e.g., a productive unit) can repay prior subsidies on behalf of the company as part or all of the sales price. Therefore, to the extent that a portion of the price paid for a privatized company can reasonably be attributed to prior subsidies, that portion of those subsidies will be extinguished."<sup>96</sup>

6.84 In commenting on the above statements by the USDOC, the United States has not offered any reason why a similar approach to the "non-distinction" between a company and its owners should not be taken in the present case. Whereas the United States indicated that "there are still other contexts where the distinction [between a company and its owners] is relevant", in doing so it only referred to the treatment of tax credits on dividends (which were apparently found by the USDOC to "benefit owners but not the company or the merchandise produced, manufactured, or exported by the company")<sup>97</sup>. The treatment of tax credits on dividends is manifestly not relevant to the present dispute.

(v) *Summary and conclusion*

6.85 In light of the above, we do not consider that the USDOC applied a correct interpretation of the Article 1.1(b) term "benefit" when finding that the "benefit" conferred on BSC by pre-1985/86 "financial contributions" by the United Kingdom Government to BSC passed through to, and continued to "benefit", UES and BSplc/BSES. For this reason, the USDOC effectively failed to establish "benefit" to UES and BSplc/BSES. Accordingly, the USDOC failed to demonstrate that any subsidy was bestowed directly or indirectly on the production, by UES and BSplc/BSES respectively, of leaded bars imported into the United States during 1994, 1995 and 1996.

6.86 We recall that, consistent with Articles 19.1, 19.4 and 21.2 of the SCM Agreement, Article VI:3 of the GATT 1994, and the object and purpose of countervailing duties as expressed in footnote 36 to Article 10, no countervailing duty may be imposed on an imported product if no (countervailable) subsidy has been bestowed directly or indirectly on *inter alia* the production of that imported product. As a result of the three administrative reviews at issue, the United States imposed countervailing duties on 1994, 1995 and 1996 imports of leaded bars, without showing that any

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<sup>96</sup> Sections of the *General Issues Appendix*, appended to *Final Affirmative Countervailing Duty Determination; Certain Steel Products from Austria*, 58 Fed. Reg. 37217, at 37262.

<sup>97</sup> See Attachment 2.8, para. 23.

subsidy had been bestowed directly or indirectly on the production of those imports. In principle, therefore, the countervailing duties imposed as a result of the USDOC's 1995, 1996 and 1997 administrative reviews are not in accordance with the premise underlying Articles 19.1, 19.4 and 21.2 of the SCM Agreement, Article VI:3 of the GATT 1994, and the object and purpose of countervailing duties as expressed in footnote 36 to Article 10. For this reason, the imposition of countervailing duties as a result of the USDOC's 1995, 1996 and 1997 administrative reviews constitutes a violation of the US obligation under Article 10 of the SCM Agreement to "take all necessary steps" to ensure that its countervailing duties are "in accordance with" with Article VI:3 of the GATT 1994 and the terms of the SCM Agreement. Accordingly, we conclude that the countervailing duties imposed as a result of the USDOC's 1995, 1996 and 1997 administrative reviews are inconsistent with Article 10 of the SCM Agreement.

### **3. The EC Article 19.4 claim**

#### **(a) Arguments of the parties**

6.87 We set forth below our understanding of the principal arguments advanced by the parties.

#### **(ii) *The European Communities***

6.88 The European Communities submits that no countervailing duties should have been levied on imports of leaded bars produced by UES or BSplc/BSES because those imports were not subsidized. By imposing countervailing duties on imports that were not subsidized, the European Communities asserts that the United States levied countervailing duties "in excess of the amount of the subsidy found to exist" in respect of those imports, contrary to Article 19.4 of the SCM Agreement.

6.89 According to the European Communities, any Article 19.4 determination of the "amount of subsidy" necessarily requires a measurement of the amount of "benefit" conferred. This requires comparing the terms of the financial contribution at issue with those that would have prevailed in the marketplace absent the subsidy. The European Communities argues that, by virtue of Article 14 of the SCM Agreement, this comparison must be made by reference to a market benchmark. Pursuant to the requisite analysis under Article 14 of the SCM Agreement, the European Communities submits that a private purchaser of a company or productive assets thereof at fair market value obtains no benefit from subsidies previously granted to the seller. Any benefit stream established for the purposes of allocating the benefit granted to the previous owner ceases to apply. Consistent with the market benchmark established in Article 14 of the SCM Agreement, the price paid in an arm's-length transaction is equal to the fair market value. Hence, for the purposes of Article 19.4 of the SCM Agreement, the "amount of the subsidy" is zero, and there can be no "subsidization per unit" of the product under investigation.

#### **(iii) *The United States***

6.90 The United States submits that the USDOC administrative reviews at issue were consistent with Article 19.4 of the SCM Agreement. According to the United States, the SCM Agreement only directs (in Article 1) that the investigating authority identify the existence of a "subsidy," including a subsidy "benefit," as of the time of the subsidy bestowal and (in Article 14) that the investigating authority measure the identified subsidy "benefit" through certain market-rate benchmarks as of the time of the subsidy bestowal.

#### **(b) Evaluation by the Panel**

6.91 The European Communities also challenges the consistency of the three administrative reviews at issue with Article 19.4 of the SCM Agreement. The European Communities' Article 19.4 claim repeats many of the arguments advanced in support of its Article 10 claim. We note that a

panel "need only address those claims which must be addressed in order to resolve the matter in issue in the dispute."<sup>98</sup> Since we have already found that the three administrative reviews at issue, and the countervailing duties to which they gave rise, are inconsistent with Article 10 of the SCM Agreement, we do not consider it necessary to address the European Communities' Article 19.4 claim.

## VII. CONCLUSION

7.1 For the above reasons, we conclude that by imposing countervailing duties on 1994, 1995 and 1996 imports of leaded bars produced by UES and BSplc/BSES respectively, the United States violated Article 10 of the SCM Agreement.

7.2 In light of Article 3.8 of the DSU, we therefore conclude that there is nullification or impairment of the benefits accruing to the complainant under the GATT 1994.

## VIII. RECOMMENDATION

8.1 Consistent with the first sentence of Article 19.1 of the DSU, we recommend that the United States bring the aforementioned measures into conformity with the SCM Agreement.

8.2 By virtue of the second sentence of Article 19.1 of the DSU, we may "suggest" ways in which the United States could implement our recommendation. The European Communities asked the Panel "to suggest that the United States amend its countervailing duty laws to recognize the principle that a privatization at market price extinguishes subsidies." The European Communities has not identified any provision of US law that **requires** the imposition of countervailing duties in the circumstances of the present dispute. Thus, we are unable to make the suggestion requested by the European Communities. However, we note that the United States has continued to apply its change-in-ownership methodology during the course of the present dispute.<sup>99</sup> We would suggest that the United States takes all appropriate steps, including a revision of its administrative practices, to prevent the aforementioned violation of Article 10 of the SCM Agreement from arising in the future.

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<sup>98</sup> *United States - Measures Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, adopted 23 May 1997, p. 19.

<sup>99</sup> The USDOC recently published the results of its 1998 administrative review of the 1992 *Leaded Bars* determination (see 64 Fed. Reg., Number 154).