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1 ARTICLE 1

1.1 Text of Article 1

Article 1

Definition of a Subsidy

1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if:

- (a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:
- (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);
 - (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits)¹;

*(footnote original)*¹ In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.

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

or

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

and

- (b) a benefit is thereby conferred.

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

1.2 General

1. In *US – Carbon Steel (India)*, the Appellate Body noted that "Article 1.1 of the SCM Agreement stipulates that a 'subsidy' shall be deemed to exist if there is a 'financial contribution by a government or any public body' and 'a benefit is thereby conferred'".¹

1.2.1 Distinction between "financial contribution" and "benefit"

2. In *Brazil – Aircraft*, the Appellate Body emphasized that "a 'financial contribution' and a 'benefit' [are] two separate legal elements in Article 1.1 of the *SCM Agreement*, which *together* determine whether a subsidy *exists*".²

3. Along the same lines, the Panel in *US – Export Restraints* emphasized the distinction between "financial contribution" and "benefit":

"Article 1.1 makes clear that the definition of a subsidy has two distinct elements (i) a financial contribution (or income or price support), (ii) which confers a benefit. The Appellate Body emphasised this point in *Brazil – Aircraft*, stating that financial contribution and benefit are 'separate legal elements in Article 1.1 ... which *together*

¹ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.8.

² Appellate Body Report, *Brazil – Aircraft*, para. 157.

determine whether a 'subsidy' exists'³, which the panel in that case had erroneously blended together by importing the concept of benefit into the definition of financial contribution."⁴

4. In *US – Softwood Lumber IV*, the Appellate Body referred again to the two distinct elements:

"The concept of subsidy defined in Article 1 of the *SCM Agreement* captures situations in which something of economic value is transferred by a government to the advantage of a recipient. A subsidy is deemed to exist where two distinct elements are present.⁵ First, there must be a financial contribution by a government, or income or price support. Secondly, any financial contribution, or income or price support, must confer a benefit."⁶

1.3 Article 1.1(a)(1): "financial contribution"

1.3.1 General

5. In *US – Large Civil Aircraft (2nd complaint)*, the Panel observed that "Article 1.1(a)(1) is a definitional provision that sets forth an exhaustive, closed list ('... i.e. where ...') of the types of transactions that constitute financial contributions under the *SCM Agreement*".⁷ The Appellate Body shared the same observation when providing its analysis of the general architecture and structure of that provision:

"Article 1.1(a)(1) defines and identifies the government conduct that constitutes a financial contribution for purposes of the *SCM Agreement*. Subparagraphs (i)-(iv) exhaust the types of government conduct deemed to constitute a financial contribution. This is because the introductory chapeau to the subparagraphs states that 'there is a financial contribution by a government ..., i.e. where:'. Some of the categories of conduct—for instance those specified in subparagraphs (i) and (ii)—are described in general terms with illustrative examples that provide an indication of the common features that characterize the conduct referred to more generally. Article 1.1(a)(1), however, does not explicitly spell out the intended relationship between the constituent subparagraphs. Finally, the subparagraphs focus primarily on the action taken by the government or a public body."⁸

6. In *US – Export Restraints*, the Panel considered the negotiating history of Article 1 and found that the inclusion of "financial contribution" in the text of the provision was meant to guarantee that not all government measures that confer benefits would be considered to be subsidies:

"The negotiating history of Article 1 confirms our interpretation of the term 'financial contribution'. This negotiating history demonstrates, in the first place, that the requirement of a financial contribution from the outset was intended by its proponents precisely to ensure that not all government measures that conferred benefits could be deemed to be subsidies. This point was extensively discussed during the negotiations, with many participants consistently maintaining that only government actions constituting financial contributions should be subject to the multilateral rules on subsidies and countervailing measures.

...

[T]he negotiating history confirms that the introduction of the two-part definition of subsidy, consisting of 'financial contribution' and 'benefit', was intended specifically to prevent the countervailing of *benefits* from any sort of (formal, enforceable)

³ (footnote original) Appellate Body Report on *Brazil – Aircraft*, para. 157 (emphasis in original).

⁴ Panel Report, *US – Exports Restraints*, para. 8.20.

⁶ Appellate Body Report, *US – Softwood Lumber IV*, para. 51.

⁷ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.955.

⁸ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 614.

government measures, by restricting to a finite list the *kinds* of government measures that would, if they conferred benefits, constitute subsidies. The negotiating history confirms that items (i)-(iii) of that list limit these kinds of measures to the transfer of economic resources from a government to a private entity. Under subparagraphs (i)-(iii), the government acting on its own behalf is effecting that transfer by directly providing something of value – either money, goods, or services – to a private entity. Subparagraph (iv) ensures that the same kinds of *government* transfers of economic resources, when undertaken through explicit *delegation of those* functions to a private entity, do not thereby escape disciplines."⁹

7. In *US – Softwood Lumber IV*, the Appellate Body stated that:

"An evaluation of the existence of a financial contribution involves consideration of the nature of the transaction through which something of economic value is transferred by a government. A wide range of transactions falls within the meaning of 'financial contribution' in Article 1.1(a)(1). According to paragraphs (i) and (ii) of Article 1.1(a)(1), a financial contribution may be made through a direct transfer of funds by a government, or the foregoing of government revenue that is otherwise due. Paragraph (iii) of Article 1.1(a)(1) recognizes that, in addition to such monetary contributions, a contribution having financial value can also be made *in kind* through governments providing goods or services, or through government purchases. Paragraph (iv) of Article 1.1(a)(1) recognizes that paragraphs (i) – (iii) could be circumvented by a government making payments to a funding mechanism or through entrusting or directing a private body to make a financial contribution. It accordingly specifies that these kinds of actions are financial contributions as well. This range of government measures capable of providing subsidies is broadened still further by the concept of 'income or price support' in paragraph (2) of Article 1.1(a)."¹⁰

8. However, in *US – Softwood Lumber IV* the Appellate Body also noted its agreement with the Panel in *US – Export Restraints* that:

"[N]ot all government measures capable of conferring benefits would necessarily fall within Article 1.1(a). If that were the case, there would be no need for Article 1.1(a), because all government measures conferring benefits, *per se*, would be subsidies. In this regard, we find informative the discussion of the negotiating history of the *SCM Agreement* contained in the panel report in *US – Export Restraints*."¹¹

9. In *Canada – Renewable Energy*, the Appellate Body provided the following guidance on how to make the proper legal characterization of a transaction under Article 1.1(a)(1):

"When determining the proper legal characterization of a measure under Article 1.1(a)(1) of the SCM Agreement, a panel must assess whether the measure may fall within any of the types of financial contributions set out in that provision. In doing so, a panel should scrutinize the measure both as to its design and operation and identify its principal characteristics. Having done so, the transaction may naturally fit into one of the types of financial contributions listed in Article 1.1(a)(1). However, transactions may be complex and multifaceted. This may mean that different aspects of the same transaction may fall under different types of financial contribution. It may also be the case that the characterization exercise does not permit the identification of a single category of financial contribution and, in that situation, as described in the *US – Large Civil Aircraft (2nd complaint)* Appellate Body report, a transaction may fall under more than one type of financial contribution. We note, however, that the fact that a transaction may fall under more than one type of financial contribution does not mean that the types of financial contributions set out in Article 1.1(a)(1) are the same or that the distinct legal concepts set out in this provision would become redundant, as the Panel suggests. We further observe that, in *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body did not address the question of whether, in the

⁹ Panel Report, *US – Exports Restraints*, paras. 8.65 and 8.73.

¹⁰ Appellate Body Report, *US – Softwood Lumber IV*, para. 52.

¹¹ Panel Report, *US – Softwood Lumber IV*, fn 35.

situation described above, a panel is under an obligation to make findings that a transaction falls under more than one subparagraph of Article 1.1(a)(1)."¹²

10. In *US – Softwood Lumber VII*, the Panel noted the possibility that a particular transaction may constitute more than one type of financial contribution under Article 1.1(a)(1):

"Article 1.1(a)(1) is not explicit as to the relationship between the subparagraphs; the structure of the provision does not exclude that there may be circumstances where a transaction may be covered by more than one subparagraph."¹³

11. The Panel noted this possibility in a situation where an investigating authority (the USDOC) had classified a financial contribution in the form of revenue foregone under Article 1.1(a)(1)(ii), and the complainant argued before the Panel that the investigating authority should have classified the financial contribution as the purchase of goods under Article 1.1(a)(1)(iii).¹⁴ The Panel ultimately decided, nevertheless, that the issue before it was not whether a financial contribution could be classified as two types of financial contributions at the same time, but whether the investigating authority had misclassified the financial contribution at issue as revenue foregone:

"We recall that Article 1.1(a)(1) does not preclude circumstances where a transaction may be characterized under more than one subparagraph of that provision. However, the issue before us is not whether the LIREPP might *also* be characterized as a purchase of goods under Article 1.1(a)(1)(iii). The issue before us is whether the USDOC erred in characterizing the LIREPP as revenue foregone, rather than the purchase of goods. The United States argues that the amount of the Net LIREPP credit was separate and apart from any purchases of renewable energy from the LIREPP participants, and that the USDOC was therefore correct in treating the amounts as revenue foregone."¹⁵

1.3.2 "by a government or any public body"

1.3.2.1 "government"

12. In *US – Countervailing Measures (China)*, the Appellate Body stated that there is "a single legal standard that defines the term 'government' under the SCM Agreement". It also pointed out that this term, as defined in Article 1.1(a)(1) of the SCM Agreement, "encompasses both the government in the 'narrow sense' and 'any public body within the territory of a Member'".¹⁶

1.3.2.2 "public body"

13. In *Korea – Commercial Vessels*, the European Communities argued that the Export-Import Bank of Korea (KEXIM) was a public body on the grounds that, inter alia, it was created and operated on the basis of a public statute giving the GOK control over its decision-making. The Panel agreed with the EC that KEXIM was a public body because it was controlled by government (or other public bodies), and that KAMCO, KDB and IBK were public bodies also, because they were controlled by the Korean government:

"[A]n entity will constitute a 'public body' if it is controlled by the government (or other public bodies). If an entity is controlled by the government (or other public bodies), then any action by that entity is attributable to the government, and should therefore fall within the scope of Article 1.1(a)(1) of the *SCM Agreement*."¹⁷

14. In *US – Anti-Dumping and Countervailing Duties (China)*, the Appellate Body reversed the Panel's finding that the term "public body" in Article 1.1(a)(1) of the SCM Agreement means "any entity controlled by a government", and found instead that the term "public body" in the context of

¹² Appellate Body Report, *Canada – Renewable Energy*, para. 5.120.

¹³ Panel Report, *US – Softwood Lumber VII*, para. 7.692.

¹⁴ Panel Report, *US – Softwood Lumber VII*, paras. 7.686-7.687.

¹⁵ Panel Report, *US – Softwood Lumber VII*, para. 7.702.

¹⁶ Appellate Body Report, *US – Countervailing Measures (China)*, para. 4.42. See also Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 286.

¹⁷ Panel Report, *Korea – Commercial vessels*, para. 7.50.

Article 1.1.(a)(1) of the SCM Agreement covers only those entities that possesses, exercise or are vested with governmental authority:

"Having completed our analysis of the interpretative elements prescribed by Article 31 of the *Vienna Convention*, we reach the following conclusions. We see the concept of 'public body' as sharing certain attributes with the concept of 'government'. A public body within the meaning of Article 1.1.(a)(1) of the *SCM Agreement* must be an entity that possesses, exercises or is vested with governmental authority. Yet, just as no two governments are exactly alike, the precise contours and characteristics of a public body are bound to differ from entity to entity, State to State, and case to case. Panels or investigating authorities confronted with the question of whether conduct falling within the scope of Article 1.1.(a)(1) is that of a public body will be in a position to answer that question only by conducting a proper evaluation of the core features of the entity concerned, and its relationship with government in the narrow sense.

In some cases, such as when a statute or other legal instrument expressly vests authority in the entity concerned, determining that such entity is a public body may be a straightforward exercise. In others, the picture may be more mixed, and the challenge more complex. The same entity may possess certain features suggesting it is a public body, and others that suggest that it is a private body.¹⁸ We do not, for example, consider that the absence of an express statutory delegation of authority necessarily precludes a determination that a particular entity is a public body. What matters is *whether* an entity is vested with authority to exercise governmental functions, rather than *how* that is achieved. There are many different ways in which government in the narrow sense could provide entities with authority. Accordingly, different types of evidence may be relevant to showing that such authority has been bestowed on a particular entity. Evidence that an entity is, in fact, exercising governmental functions may serve as evidence that it possesses or has been vested with governmental authority, particularly where such evidence points to a sustained and systematic practice. It follows, in our view, that evidence that a government exercises meaningful control over an entity and its conduct may serve, in certain circumstances, as evidence that the relevant entity possesses governmental authority and exercises such authority in the performance of governmental functions. We stress, however, that, apart from an express delegation of authority in a legal instrument, the existence of mere formal links between an entity and government in the narrow sense is unlikely to suffice to establish the necessary possession of governmental authority. Thus, for example, the mere fact that a government is the majority shareholder of an entity does not demonstrate that the government exercises meaningful control over the conduct of that entity, much less that the government has bestowed it with governmental authority. In some instances, however, where the evidence shows that the formal indicia of government control are manifold, and there is also evidence that such control has been exercised in a meaningful way, then such evidence may permit an inference that the entity concerned is exercising governmental authority."¹⁹

15. In *US – Carbon Steel (India)*, the Appellate Body referred to its findings in *US – Anti-Dumping and Countervailing Duties (China)* and recalled that "the mere ownership or control over an entity by a government, without more, is not sufficient to establish that the entity is a public body".²⁰ The Appellate Body added:

"In determining whether or not a specific entity is a public body, it may be relevant to consider 'whether the functions or conduct are of a kind that are ordinarily classified

¹⁸ (footnote original) In this context, we note that the panel in *US – Countervailing Duty Investigation on DRAMS* commented, with respect to certain entities, that the USDOC had treated as "private bodies", that, "[d]epending on the circumstances", the evidence "might well have justified treatment of such creditors as public bodies." (Panel Report, *US – Countervailing Duty Investigation on DRAMS*, footnote 29 to para. 7.8) While we do not agree with that panel's implication that the particular evidence to which it referred—evidence of government ownership—could be decisive, we do consider that the statement illustrates that the analysis of whether the conduct of a particular entity is conduct of the government or a public body or conduct of a private body is indeed multi-faceted and that an entity may display characteristics pointing into different directions.

¹⁹ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, paras. 317-318.

²⁰ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.10.

as governmental in the legal order of the relevant Member.' The ... classification and functions of entities within WTO Members generally may also bear on the question of what features are normally exhibited by public bodies."²¹

16. In the same case, the Appellate Body rejected India's argument that an entity must have the power to regulate, control, or supervise individuals, or otherwise restrain conduct of others in order to be a public body:

"Although certain entities that are found to constitute public bodies may possess the power to regulate, we do not see why an entity would necessarily have to possess this characteristic in order to be found to be vested with governmental authority or exercising a governmental function and therefore to constitute a public body."²²

17. The Panel in *US – Pipes and Tubes (Turkey)* rejected the US Department of Commerce's (USDOC) assertion that Erdemir and Isdemir of Türkiye were public bodies through Ordu Yardimlasma Kurumu (OYAK). OYAK held a majority of shares in Erdemir, which in turn owns more than 92% of Isdemir. The Panel stated:

"We do not consider the fact that OYAK's governing bodies are comprised of military and certain governmental personnel, which elect the eight-person board of directors, that OYAK is ensured mandatory contributions for pension purposes, and that OYAK may benefit from its certain property and tax status, is sufficient to establish that OYAK acts pursuant to governmental authority or is under the meaningful control of the GOT. The Appellate Body has explained that evidence of 'formal indicia of control', such as a government's power to appoint and nominate directors to the board of an entity may be relevant to the assessment of whether the conduct of an entity is that of a public body. However, the Appellate Body also observed that 'a government's power to appoint directors to the board of an entity and the issue of whether those directors are independent, would seem to be distinct factors' in assessing the governmental character of an entity. We see nothing in the evidence that the USDOC considered in its analysis of OYAK to suggest that military and government personnel within OYAK have made decisions under the direction of the GOT in pursuit of governmental economic policies."²³

18. In *US – Carbon Steel (India) (Article 21.5 – India)*, the Panel did not agree with India's contention that Article 1.1(a)(1) creates a "duty/obligation" to both seek and accept evidence when determining whether a specific entity is a public body. The Panel stated:

"[I]f an investigating authority does not possess sufficient evidence on the record to reach a determination, it may need to seek or accept additional evidence in order to be capable of providing a 'reasoned and adequate' explanation that satisfies the requirements of a substantive obligation. However, it does not follow that there is a standalone obligation in Article 1.1(a)(1) to seek or accept evidence separate from the basic requirement to provide a 'reasoned or adequate' explanation."²⁴

1.3.2.2.1 Legal standard

19. Addressing the legal standard to be applied by investigating authorities in public body determinations, the compliance Panel in *US – Countervailing Measures (China) (Article 21.5 – China)* recognized that the disagreement between the parties was "whether Article 1.1(a)(1) requires an investigating authority to establish that an entity is fulfilling a government function when providing a particular financial contribution in order to determine that the entity possesses, exercises or is vested with governmental authority."²⁵

20. The Panel disagreed with China's argument that the proper question for an investigating authority is whether an entity is performing a government function when it engages in relevant

²¹ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.9.

²² Appellate Body Report, *US – Carbon Steel (India)*, para. 4.17.

²³ Panel Report, *US – Pipes and Tubes (Turkey)*, para. 7.39.

²⁴ Panel Report, *US – Carbon Steel (India) (Article 21.5 – India)*, para. 7.73.

²⁵ Panel Report, *US – Countervailing Measures (China) (Article 21.5 – China)*, para. 7.24.

conduct under Article 1.1(a)(1), that is when it provides a financial contribution. The Panel pointed out that "[i]n a public body analysis, an investigating authority must give due consideration to *all* relevant facts regarding the characteristics and functions of an entity as appropriate in the particular circumstances of the case."²⁶ The Panel disagreed with "China's understanding of the legal standard for public body determinations in so far as it would require a particular degree or nature of connection in all cases between an identified government function and the particular financial contribution at issue."²⁷ Rather, the Panel considered that "the applicable legal standard requires a holistic assessment by an investigating authority of the evidence before it. Similarly, a Panel must consider whether the public body determination is based on relevant evidence and adequate explanation in assessing whether the investigating authority properly concluded that entities possessed, exercised, or were vested with governmental authority to perform a government function."²⁸

21. The Appellate Body in *US – Countervailing Measures (China)* (Article 21.5 – China) upheld the Panel's findings about public body and stated that the focus of the public body analysis is "on the *entity* ..., its core characteristics, and its relationship with government",²⁹ while "the conduct of an entity – particularly when it points to a 'sustained and systematic practice' – is *one* of the various types of evidence that may shed light on the core characteristics of an entity and its relationship with government in the narrow sense."³⁰

22. The Appellate Body further considered that "[t]his focus on the entity, as opposed to the conduct alleged to give rise to a financial contribution, comports with the fact that a 'government' (in the narrow sense) and a 'public body' share a 'degree of commonality or overlap in their essential characteristics' – i.e. they are both 'governmental' in nature",³¹ and added that, similarly to a government, "*all* conduct" of an entity established to be a public body "shall be attributable to the Member concerned for purposes of Article 1.1(a)(1)."³² In this regard, the Appellate Body rejected China's argument that, in considering whether the relevant entities are public bodies, a government must be found to exercise "meaningful control" over the conduct at issue under Article 1.1(a)(1)(i)-(iii) or the first clause of subparagraph (iv), and stated that this type of inquiry resembles more the inquiry of an investigating authority concerning the second clause of Article 1.1(a)(1)(iv) of the SCM Agreement.³³ The Appellate Body pointed out that:

"[W]hen it is alleged that the conduct of a private body gives rise to a financial contribution, an investigating authority must establish an *additional* 'link between the government and *that conduct*' in the form of 'entrustment or direction'. ... By contrast, if it is established that an entity is a public body within the domestic system of a Member, then the conduct of that entity is *directly* attributable to the Member concerned."³⁴

23. In *US – Countervailing Measures (China)* (Article 21.5 – China), one member of the Division expressed a separate opinion regarding what the Appellate Body has treated as an essential criterion for determining whether an entity is a public body, namely, the requirement that the entity "possesses, exercises or is vested with governmental authority".³⁵ The separate opinion noted that this phrase, which was used by the majority in this case, was "rigid and limiting".³⁶ The member of the Division thereby considered that the text of Article 1.1(a)(1) of the SCM Agreement makes an unqualified "collective reference to 'a government or any public body' as comprising the entity 'government'",³⁷ and further clarified:

"Whether an entity is a public body must be determined on a case-by-case basis with due regard being had for the characteristics of the relevant entity, its relationship with

²⁶ Panel Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 7.32.

²⁷ Panel Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 7.36.

²⁸ Panel Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 7.30.

²⁹ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.100.

³⁰ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.101.

³¹ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.100.

³² Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.100.

³³ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.103.

³⁴ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.103.

³⁵ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.245.

³⁶ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.245.

³⁷ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.247.

the government, and the legal and economic environment prevailing in the country in which the entity operates. Just as no two governments are exactly alike, the precise contours and characteristics of a public body are bound to differ from entity to entity, State to State, and case to case. An entity may be found to be a public body when the government has the ability to control that entity and/or its conduct to convey financial value. There is no requirement for an investigating authority to determine in each case whether the investigated entity 'possesses, exercises or is vested with governmental authority'.³⁸

24. The Panel in *US – Carbon Steel (India)* (Article 21.5 – India) found that Article 1.1(a)(1) does not contain a stand-alone obligation for investigating authorities to seek or accept evidence (in this case, concerning the existence of a public body) apart from the obligation to base its determinations on reasoned and adequate explanations. The Panel noted:

"Rather, the presence of sufficient evidence on the record is a corollary of an investigating authority being able to undertake the evaluation necessary to comply with the legal standard for a substantive obligation. If an investigating authority does not possess sufficient evidence on the record to reach a determination, it may need to seek or accept additional evidence in order to be capable of providing a 'reasoned and adequate' explanation that satisfies the requirements of a substantive obligation. However, it does not follow that there is a standalone obligation in Article 1.1(a)(1) to seek or accept evidence separate from the basic requirement to provide a 'reasoned and adequate' explanation."³⁹

1.3.2.2.2 Evidentiary standard

25. The Appellate Body has found that a determination of whether conduct, falling within the scope of Article 1.1(a)(1), is that of a public body requires "a proper evaluation of the core features of the entity concerned, and its relationship with the government in the narrow sense".⁴⁰ In addition, investigating authorities should consider "all relevant characteristics of the entity" and should therefore avoid focusing exclusively or unduly on any single characteristic without affording due consideration to others that may be relevant.⁴¹

26. In *US – Carbon Steel (India)*, the Appellate Body disagreed with the Panel's interpretation that the Appellate Body in *US – Anti-Dumping and Countervailing Duties (China)* had "implicitly accepted" that an investigating authority's public body determination can rely exclusively on a single aspect of the entity's relationship with a government, namely, whether an entity is controlled by a government in the sense that the chief executives of the entity are "government appointed".⁴²

27. The Panel in *US – Carbon Steel (India)* (Article 21.5 – India) rejected India's argument that the Panel could permissibly take into account information submitted in the course of the investigation at issue but which the USDOC was legally precluded from taking into account:

"Although the 'new factual information' was technically on the record, the key point is that, according to the United States, the USDOC was legally precluded from having regard to this information in its investigation. The oft-used formulation of a panel's standard of review under the SCM Agreement is that 'a panel must examine whether, *in the light of the evidence on the record*, the conclusions reached by the investigating authority are reasoned and adequate'. The 'new factual information' cannot be said to be 'on the record' for this purpose. This is because the conclusions of the USDOC were not reached in light of that information, since the USDOC was legally precluded from considering that information.

India contended that the Panel could permissibly take the 'new factual information' into account. For India, 'the evidence was already on record and within the knowledge

³⁸ Appellate Body Report, *US – Countervailing Measures (China)* (Article 21.5 – China), para. 5.248.

³⁹ Panel Report, *US – Carbon Steel (India)* (Article 21.5 – India), para. 7.26.

⁴⁰ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.43 and 4.24.

⁴¹ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 319.

⁴² Appellate Body Report, *US – Carbon Steel (India)*, para. 4.45.

of the United States'. India explained that the corresponding exhibits had been submitted in the original panel proceedings, and also that some of the information could be found in weblinks that had been provided in the underlying investigations, while other aspects of the information pertained to concepts, terms, or evidence that the USDOC had itself referenced in its own documents and determinations. None of the reasons offered by India rebut the proposition that the 'new factual information' was not on the record *for the purpose of the USDOC's evaluation*, and thus is not permissibly within the purview of this Panel's evaluation. To find otherwise would be to invite an impermissible *de novo* review – that is, to take into account new evidence that was not before the investigating authority for the purposes of its evaluation."⁴³

1.3.2.3 Financial contribution "by" individual public entities or private bodies

28. In *Korea – Commercial Vessels*, the Panel rejected Korea's argument that there were no financial contributions "by" individual public bodies or private bodies in the restructuring of the Korean shipyards because those restructurings were effected collectively, either by the creditors' councils, meetings of interested parties, or court decisions. The Panel concluded that where a public body participates in a loan agreed by a creditors' council, the part of the loan attributable to the public body constitutes an individual financial contribution by that public body under Article 1.1(a) of the SCM Agreement. The Panel considered that:

"[E]ntities participating in a financial contribution must assume responsibility for that participation. Thus, to the extent that a public body participates in a loan agreed by a creditors' council, that part of the loan attributable to the public body may be treated as an individual financial contribution by that public body falling within the scope of Article 1.1(a) of the *SCM Agreement*. Otherwise the disciplines of the *SCM Agreement* could be easily circumvented by groups of public bodies deciding collectively, or under court approval, to provide financial contributions."⁴⁴

1.3.3 Article 1.1(a)(1)(i): transfer of funds

1.3.3.1 "a government practice"

29. The Panel in *Korea – Commercial Vessels* found that the loans and loan guarantees at issue fell under Article 1.1(a)(1)(i), rejecting Korea's argument that "financial contribution" exists only if a public body is engaged in "government practice," such as regulation or taxation:

"Article 1.1(a)(1) states in relevant part that term 'government' refers to both 'government' and 'public body'. Since the phrase 'government practice' in Article 1.1(a)(1)(i) therefore refers to the practice of both governments and public bodies, the practice at issue need not necessarily be purely "governmental" in the narrow sense advocated by Korea. In this regard, we consider that the concept of 'financial contribution' is writ broadly to cover government and public body actions that might involve subsidization. Whether the government or public body action in fact gives rise to subsidization will depend on whether it gives rise to a 'benefit'. Since the concept of 'benefit' acts as a screen to filter out commercial conduct, it is not necessary to introduce such a screen into the concept of 'financial contribution'."⁴⁵

30. The Panel in *Korea – Commercial Vessels* concluded that the phrase "government practice" is used to denote the author of the action, rather than the nature of the action and that "[g]overnment practice" therefore covers all acts of governments or public bodies, irrespective of whether or not they involve the exercise of regulatory powers or taxation authority."⁴⁶

1.3.3.2 "direct transfer of funds"

31. The Appellate Body in *US – Large Civil Aircraft (2nd complaint)* stated that a "direct transfer of funds" in subparagraph (i) captures "conduct on the part of the government by which money,

⁴³ Panel Report, *US – Carbon Steel (India)* (Article 21.5 – India), paras. 7.76-7.77.

⁴⁴ Panel Report, *Korea – Commercial vessels*, paras. 7.424-425.

⁴⁵ Panel Report, *Korea – Commercial vessels*, paras. 7.28.

⁴⁶ Panel Report, *Korea – Commercial vessels*, paras. 7.29.

financial resources, and/or financial claims are made available to a recipient".⁴⁷ The Appellate Body also reiterated its previous finding in *Japan – DRAMs (Korea)* that the meaning of "funds" includes not only money, but also financial resources and other financial claims more generally.⁴⁸ Based on the examples in subparagraph (i), the Appellate Body elaborated:

"It is clear from the examples in subparagraph (i) that a direct transfer of funds will normally involve financing by the government to the recipient. In some instances, as in the case of grants, the conveyance of funds will not involve a reciprocal obligation on the part of the recipient. In other cases, such as loans and equity infusions, the recipient assumes obligations to the government in exchange for the funds provided. Thus, the provision of funding may amount to a donation or may involve reciprocal rights and obligations."⁴⁹

32. The compliance Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* concluded that the fact that some of the disbursements specifically envisaged under the A350XWB LA/MSF contracts were yet to be made did not preclude a finding that the entirety of the envisaged LA/MSF measures represented direct transfers of funds. Accordingly, the Panel reached the same conclusion as the original panel that the LA/MSF contracts at issue involved a direct transfer of funds within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement.⁵⁰

33. In *Korea – Commercial Vessels*, Korea argued that transactions involving debt-for-equity swaps and modifications of loan repayment terms are not covered by Article 1.1(a)(1)(i) because they do not involve any transfer of (new) funds. The Panel was not persuaded:

"We are not persuaded by Korea's arguments that debt-for-equity swaps and interest reductions and deferrals are not financial contributions. In the first place, we recall that there is a financial contribution in the sense of Article 1.1(a)(1)(i) of the *SCM Agreement* if there is a 'direct transfer of funds', and that grants, loans and equity infusions are listed only as three possible examples of such transfers. Thus, we view Article 1.1(a)(1) as identifying in its respective subparagraphs the kinds of instruments or transactions that could be considered to be 'financial contributions'. Of course these instruments would only be covered by the Agreement if they were made 'by a government or public body', and they would only be subsidies covered by the Agreement if they both conferred a benefit and were specific. Thus, the concept of financial contribution is but one in a set of cumulative, and independent, elements all of which must be present for a measure to be regulated by the *SCM Agreement*.

We find the examples listed in Article 1.1(a)(1)(i) to be illuminating in respect of the scope of the term 'direct transfer of funds'. Most importantly, considering the 'medium of exchange' in the listed examples, we note that all of the examples involve transfers of money ('funds'), as opposed to in-kind transfers (of goods or services, in the sense of Article 1.1(a)(1)(iii)). The fact that the listed kinds of direct transfers of funds (grants, loans and equity infusions) are identified as only examples clearly indicates that there may well be other types of instruments that would equally constitute direct transfers of funds in the sense of Article 1.1(a)(1)(i).

Turning to the particular cases of the transactions involved in the restructuring, we find that all of them are of the same nature as those explicitly listed in Article 1.1(a)(1)(i). First we note that interest reductions and deferrals are similar to new loans, as they involve a renegotiation / extension of the terms of the original loan. We see no reason why loans would constitute financial contributions while interest reductions and deferrals would not. Further, we consider that interest / debt forgiveness is comparable to a cash grant, as funds that were previously provided as a loan, against interest, are now provided for free, given the removal of the repayment obligation. All of these transactions therefore constitute direct transfers of funds in the sense of Article 1.1(a)(1)(i) of the *SCM Agreement*. Regarding debt-for-equity swaps, we note that equity infusions are explicitly listed as a type of direct transfer of funds

⁴⁷ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 614.

⁴⁸ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 614.

⁴⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 617.

⁵⁰ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.290.

in Article 1.1(a)(1)(i). Since we have also found that debt forgiveness constitutes a direct transfer of funds, we see no reason why a combination of equity infusion and debt forgiveness should fall outside the scope of that provision. The reason why creditors agree to such transactions (*i.e.*, whether or not it is in order to preserve going concern value) is not relevant to the issue of whether or not the transactions constitute financial contributions. Rather, it relates to the issue of benefit (in the sense of whether or not creditors operating on market principles would have undertaken such transactions on the same terms).⁵¹

34. The Panel in *Korea – Commercial Vessels* reasoned that equity infusions and debt-for-equity swaps have the same effect:

"Equity infusions and debt-for-equity swaps have the same effect, in the sense that equity changes hands against consideration in both cases (and subsidization arises if the amount of consideration is less than the market would have provided). Also, a debt/equity swap comprises an element of equity infusion."⁵²

35. Korea advanced a similar argument in *Japan – DRAMs (Korea)*, but that Panel was also not persuaded:

"We do not accept that the relinquishment or modification of claims may not, in certain circumstances, be treated as the transfer of new claims, giving rise to new rights and obligations. For example, once one analyses what actually occurs in the transaction, the modification of an existing loan may properly be treated as the transfer of new rights to the recipient of the modified loan. The borrower's old rights no longer exist. They have been replaced by new rights. In this sense, the modified loan may properly be treated as a new loan. Thus, the modification of a loan through debt forgiveness involves the transfer of new rights to the borrower, who is now liberated of the obligation to repay the debt, and instead has the right to use the money for free. Similarly, the modification of a loan through an extension of the loan maturity involves the transfer of new rights to the borrower, who is now entitled to borrow the money for a longer period of time. Since the new rights that are transferred in such transactions have monetary value, and may be counted in a (legal or natural) person's capital, we consider that such transactions may properly be treated as 'direct transfers of funds' in the meaning of Article 1.1(a)(1)(i) of the *SCM Agreement*. We apply the same analysis to debt-to-equity swaps, for the relinquishment and modification of claims inherent in such transactions similarly results in new rights, or claims, being transferred to the former debtor."⁵³

36. The Panel continued:

"Furthermore, we note that in *Korea-Commercial Vessels*, Korea advanced essentially the same argument that it advances here. In that case, Korea argued that the debt-to-equity swaps, interest rate reductions, interest forgiveness and interest deferral at issue did not constitute 'financial contributions' because there was 'no transfer of pecuniary value' to the companies under workout or corporate reorganization. The panel rejected Korea's argument, and found that all of those transactions involved a 'direct transfer of funds' within the meaning of Article 1.1(a)(1)(i) ...

...

We agree with this analysis by the panel in *Korea – Commercial Vessels*. We agree in particular that it is appropriate to look beyond the simple form of a transaction, and analyze its effects, in determining whether or not a transaction constitutes a 'direct transfer of funds'.⁵⁴

⁵¹ Panel Report, *Korea-Commercial Vessels*, paras. 7.411-7.413.

⁵² Panel Report, *Korea-Commercial Vessels*, para. 7.420.

⁵³ Panel Report, *Japan – DRAMs (Korea)*, para. 7.442.

⁵⁴ Panel Report, *Japan – DRAMs (Korea)*, paras. 7.443-7.444.

37. The Appellate Body upheld the findings of the Panel in *Japan – DRAMs (Korea)*. The Appellate Body reasoned that:

"In our view, the term 'funds' encompasses not only 'money' but also financial resources and other financial claims more generally. The concept of 'transfer of funds' adopted by Korea is too literal and mechanistic because it fails to encapsulate how financial transactions give rise to an alteration of obligations from which an accrual of financial resources results. We are unable to agree that direct transfers of funds, as contemplated in Article 1.1(a)(1)(i), are confined to situations where there is an incremental flow of funds to the recipient that enhances the net worth of the recipient. Therefore, the Panel did not err in finding that the JIA properly characterized the modification of the terms of pre-existing loans in the present case as a direct transfer of funds.

We observe that the words 'grants, loans, and equity infusion' are preceded by the abbreviation 'e.g.', which indicates that grants, loans, and equity infusion are cited examples of transactions falling within the scope of Article 1.1(a)(1)(i). This shows that transactions that are similar to those expressly listed are also covered by the provision. Debt forgiveness, which extinguishes the claims of a creditor, is a form of performance by which the borrower is taken to have repaid the loan to the lender. The extension of a loan maturity enables the borrower to enjoy the benefit of the loan for an extended period of time. An interest rate reduction lowers the debt servicing burden of the borrower. In all of these cases, the financial position of the borrower is improved and therefore there is a direct transfer of funds within the meaning of Article 1.1(a)(1)(i).

With respect to Korea's argument that debt-to-equity swaps cannot be considered as direct transfers of funds given that no money is transferred thereby to the recipient, the Panel reasoned that 'the relinquishment and modification of claims inherent in such transactions similarly result[] in new rights, or claims, being transferred to the former debtor.' Again, we see no error in the Panel's analysis. Debt-to-equity swaps replace debt with equity, and in a case such as this, when the debt-to-equity swap is intended to address the deteriorating financial condition of the recipient company, the cancellation of the debt amounts to a direct transfer of funds to the company."⁵⁵

38. Along the same lines, the Panel in *EC and certain member States – Large Civil Aircraft* concluded that a share transfer involved a "direct transfer of funds" within the meaning of Article 1.1(a)(1)(i):

"We now turn to the United States' claim that the 1992 acquisition by MBB of KfW's 20 percent equity interest in Deutsche Airbus was also a subsidy. We first consider whether the transfer by KfW of its shares in Deutsche Airbus to MBB is a 'financial contribution' in the sense of Article 1.1(a)(1)(i) of the SCM Agreement. The Appellate Body has indicated that the term 'funds' in Article 1.1(a)(1)(i) encompasses not only 'money' but also financial resources and other financial claims more generally.⁵⁶ We regard shares in a company as financial claims to a stream of income (in the form of dividends paid out of a company's profits) and to a share in the capital of the company on its liquidation. Therefore, we consider that shares in a company fall within the scope of the term 'funds' in Article 1.1(a)(1)(i), and that a transfer of shares falls within the scope of the term 'direct transfer of funds'. We thus conclude that the transfer by KfW of its 20 percent equity interest in Deutsche Airbus to MBB was a 'financial contribution' within the meaning of Article 1.1(a)(1)(i)."⁵⁷

39. Applying similar reasoning, the Panel in *EC and certain member States – Large Civil Aircraft* also found that the relinquishment of a government-held debt may also constitute a "direct transfer of funds" within the meaning of Article 1.1(a)(1)(i):

⁵⁵ Appellate Body Report, *Japan – DRAMs (Korea)*, paras. 250-252.

⁵⁶ (footnote original) Appellate Body Report, *Japan – DRAMs (Korea)*, para. 250.

⁵⁷ Panel Report, *EC and certain member States – Large Civil Aircraft*, para. 7.1291.

"The United States characterizes the financial contribution arising out of the 1998 debt settlement as 'debt forgiveness'. Our approach is, rather, to determine first, whether the 1998 debt settlement involves a financial contribution within the meaning of Article 1.1(a)(1) of the SCM Agreement, and second, whether that financial contribution confers a benefit on Deutsche Airbus within the meaning of Article 1.1(b) of the SCM Agreement. If we conclude that the financial contribution confers a 'benefit' on Deutsche Airbus, then it may be that the subsidy in question could be described as 'debt forgiveness' in an amount equal to the amount of benefit found to have been conferred. However, the first issue for us to determine is whether the 1998 debt settlement constitutes one of the forms of financial contribution set forth in Article 1.1(a)(1). We conclude that the 1998 debt settlement constitutes a financial contribution in the form of a 'direct transfer of funds' within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. We note that, in *Japan – DRAMS*, the Appellate Body interpreted the term 'funds' in Article 1.1(a)(1)(i) broadly, as encompassing not only 'money' but also 'financial resources and other *financial claims* more generally.' Debt owed to the government is an asset held by the government consisting of certain *financial claims* (i.e., rights to payment of money or equivalents) that the government has against a debtor. A settlement of government-held debt essentially involves the transfer to the debtor of the government's financial claims against that debtor, resulting in the cancellation of the debt. We therefore regard a settlement of debt as a 'direct transfer of funds' by a government, and thus a 'financial contribution' within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement."⁵⁸

40. In *US – Large Civil Aircraft (2nd complaint)*, in a finding that the Appellate Body subsequently declared to be moot and of no legal effect⁵⁹, the Panel stated that transactions involving purchases of services are excluded from the scope of Article 1.1(a)(1). The Panel recognized that the plain meaning of "transfer of funds" is broad, but considered it necessary to interpret the terms of Article 1.1(a)(1)(i) in their context:

"Article 1.1(a)(1)(i) provides in relevant part that a financial contribution exists where 'a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion)'. We accept that if the terms of Article 1.1(a)(1)(i) of the SCM Agreement are read in isolation, the ordinary meaning of the words 'a government practice involves a direct transfer of funds' might be broad enough to cover purchases of services. First, there is nothing in the dictionary definitions of these terms to suggest that transactions properly characterized as purchases of services fall outside of their scope: the definition of 'transfer' is 'a conveyance from one person to another', and the definition of 'funds' is 'a stock or sum of money, esp. one set apart for a particular purpose' or 'financial resources'. Second, there is no qualifying or limiting language in the text of this provision. Third, one of the examples of a 'direct transfer of funds' given in Article 1.1(a)(1)(i) is that of 'equity infusion', which refers to a situation in which a government 'purchases' something (i.e. shares in a company). Fourth, previous panels and the Appellate Body have not given a restrictive interpretation to these terms. However, the terms of Article 1.1(a)(1)(i) must be read in their context."⁶⁰

41. The Appellate Body in *US – Large Civil Aircraft (2nd complaint)* found that certain measures, joint ventures arrangements, had sufficient characteristics in common with one of the examples in subparagraph (i), equity infusions, to indicate that the measures fell within the concept of "direct transfers of funds" in Article 1.1(a)(1)(i):

"With respect to the examples in Article 1.1(a)(1)(i), we observe several similarities between the collaborative undertakings that are the NASA/USDOD measures before us and equity infusions. We recall that, in the case of an equity infusion, a government's provision of capital to a recipient is made in return for the acquisition of shares. The provider of the capital thereby makes an investment in the recipient enterprise, and will be entitled to the dividends or any capital gains attributable to that

⁵⁸ Panel Report, *EC and certain member States – Large Civil Aircraft*, para. 7.1318.

⁵⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 620.

⁶⁰ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.954.

investment. The return of the investment will depend on the success of the recipient enterprise. At the time the government provides the capital, it does not know how the recipient enterprise will perform. The equity investor enjoys a return on its capital to the extent the enterprise succeeds, and suffers losses in capital to the extent it fails. This type of transaction can be replicated through other arrangements, such as by means of a joint venture.

Like equity investors, NASA and the USDOD provide funding. This funding is provided in the expectation of some kind of return. In the case of NASA and USDOD funding to Boeing, the return is not financial, but rather takes the form of scientific and technical information, discoveries, and data expected to result from the research performed. Again, like equity investors, NASA and the USDOD have no certainty at the time they commit the funding that the research will be successful. Success will depend on whether any inventions are discovered and the usefulness of the data collected, as well as the scientific and technical information produced. NASA's and the USDOD's risks are limited to the amount of money they contribute and the opportunity cost of the other support they provide to the project, much like an equity investor. And like some equity investors, NASA and the USDOD contribute to the project by providing access to facilities, equipment, and employees."⁶¹

42. The Panel in *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU) did not consider the allocation of intellectual property rights as between the United States' Department of Defence (DOD) and aerospace company Boeing transformed their relationship, under DOD procurement contracts at issue, from purchaser and seller to joint venture partners.⁶² The Panel further explained:

"This different 'balance' of allocation of intellectual property rights that results from the performance of work under a DOD procurement contract also affects our assessment of whether DOD and Boeing can be said to share in the 'risks and rewards' of the commissioned R&D. While the outcome of R&D performed under many of the DOD procurement contracts ... is uncertain, the risks and rewards are borne principally by DOD."⁶³

43. The Panel in *India – Export Related Measures* found that the provision of scrips by the Government of India as a reward for exports under the Merchandise Exports from India Scheme (MEIS) constituted a direct transfer of funds within the meaning of Article 1.1(a)(i) of the SCM Agreement. According to the Panel, "both because scrips can be used to pay for customs duties and other liabilities *vis-à-vis* the Government [of India], and because they can be sold to third party recipients for consideration, they are 'financial resources and/or financial claims', i.e. 'funds' within the meaning of Article 1.1(a)(1)(i)."⁶⁴

44. While noting that the examples in Article 1.1(a)(1)(i) are not exhaustive, the Panel also examined, to address India's arguments, the relationship between those examples and the MEIS scrips:

"The first example, i.e. 'grants', consists of transactions in which 'money or money's worth is given to a recipient, normally without an obligation or expectation that anything will be provided to the grantor in return'⁶⁵; in contrast, the other two examples, 'loans' and 'equity infusion', 'are characterized by reciprocity'.⁶⁶ We note that, when India grants MEIS scrips, it provides "money's worth ... to a recipient". While past exports trigger the granting of scrips, there is no obligation or expectation that any form of return will be provided to the Government of India for the scrips. Further, grants can be 'conditional', as MEIS scrips are.⁶⁷ Therefore, MEIS scrips have

⁶¹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 622-623.

⁶² Panel Report, *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU), para. 8.370.

⁶³ Panel Report, *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU), para. 8.368.

⁶⁴ Panel Report, *India – Export Related Measures*, para. 7.432.

⁶⁵ (footnote original) Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 616.

⁶⁶ (footnote original) Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 616.

⁶⁷ (footnote original) Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, fn 1292.

significant commonalities with grants, which further confirms that they do fall within subparagraph (i)."⁶⁸

45. In addition, the Panel rejected India's argument that MEIS scrips cannot fall under subparagraph (i) because they fall under subparagraph (ii) of Article 1.1(a)(1). The Panel noted that the two subparagraphs, while being context for each other, are not mutually exclusive. Therefore, for the finding that MEIS scrips fall within subparagraph (i) to stand, there was no need to exclude that aspects of the measure may fall under subparagraph (ii).⁶⁹

1.3.3.2.1 "e.g. grants, loans, and equity infusion"

46. The Appellate Body observed, in *Japan – DRAMs (Korea)* and *US – Large Civil Aircraft (2nd complaint)*, that the phrase "e.g. grants, loans, and equity infusion" in Article 1.1(a)(1)(i) represents examples of direct transfers of funds:

"[T]he fact that the words 'grants, loans, and equity infusion' are preceded by the abbreviation 'e.g.', indicates that they are cited as examples of transactions falling within the scope of Article 1.1(a)(1)(i). These examples, which are illustrative, do not exhaust the class of conduct captured by subparagraph (i). The inclusion of specific examples nevertheless provides an indication of the types of transactions intended to be covered by the more general reference to 'direct transfer of funds'."⁷⁰

47. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body provided a brief explanation for each of these three types of direct transfer of funds. With regards to "grants", the Appellate Body noted that, in such a transaction, money or money's worth is given to a recipient, normally without an obligation or expectation that anything will be provided to the grantor in return. It further noted that grants can take many forms. For example, some conditional grants require the recipient to use the funds for a specific purpose and other conditional grants require a recipient to itself raise part of the funds needed for a project.⁷¹

48. "Loans" and "equity infusions", as explained by the Appellate Body in the same case, are characterized by reciprocity:

"With a loan, the lender lends money or money's worth on the basis that the principal, along with interest as may be agreed, is repaid. Under a loan, the lender will usually earn a return on the amount borrowed. In the case of an equity infusion, a government's provision of capital to a recipient is made in return for the acquisition of shares. The provider of the capital thereby makes an investment in the recipient enterprise⁷² and will be entitled to the dividends or any capital gains attributable to that investment. The returns on the investment will depend on the success of the recipient enterprise. At the time the government provides the capital, it does not know how the recipient enterprise will perform. The equity investor enjoys a return on its capital to the extent the enterprise succeeds, and suffers losses in capital to the extent it fails."⁷³

49. The Panel in *US – Softwood Lumber VII* agreed with the Appellate Body's understanding of the term "grant" set forth in Article 1.1(a)(1)(i) as the act of giving "money or money's worth" to a recipient without any obligation or expectation that anything will be provided to the grantor in return:

⁶⁸ Panel Report, *India – Export Related Measures*, para. 7.436.

⁶⁹ Panel Report, *India – Export Related Measures*, para. 7.437.

⁷⁰ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 614. See also Appellate Body Report, *Japan – DRAMs (Korea)*, para. 251.

⁷¹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 616 and fn 1292.

⁷² (footnote original) This notion of an investment through an equity infusion is reinforced by Article 14(a) of the *SCM Agreement*, which expressly provides that the determination of whether an equity infusion confers a benefit must be made based on whether the "investment decision" is *inconsistent* with the "usual investment practice" of private investors in the territory of the Member.

⁷³ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 616.

"Article 1.1 of the SCM Agreement stipulates that a subsidy shall be deemed to exist if there is a financial contribution by a government whereby a benefit is conferred on the recipient of the financial contribution. Article 1.1(a)(1)(i) provides that a financial contribution could be made in the form of a direct transfer of funds and includes grants as an example of a direct transfer of funds. The Appellate Body has found that a grant normally exists when money or money's worth is given to a recipient without an obligation or expectation that anything will be provided to the grantor in return. We agree with this finding of the Appellate Body. We further note that the United States and Canada both agree that a grant exists for purposes of Article 1.1(a)(1)(i) when the government confers something on a recipient without getting anything in return."⁷⁴

50. The Panel ultimately considered that the USDOC erred in characterizing the financial contribution as a "grant" under Article 1.1(a)(1)(i) because the legal framework governing the alleged financial contribution had obliged the company at issue "to undertake certain silviculture and forest management obligations" and had obliged New Brunswick to reimburse the company at issue for the performance of these obligations:

"We note that even though the CLFA and the FMA contain provisions that oblige JDIL to undertake certain silviculture and forest management obligations, the same legal instruments also provide that New Brunswick shall reimburse JDIL for the performance of such obligations. We consider that the fact that the relevant obligations as well as the reimbursement for the performance of those obligations are foreseen in the same legal instruments undermines the USDOC's characterization of the reimbursement as a grant. This is because the obligations and the reimbursement are both parts of the set of terms based on which New Brunswick provided Crown timber to JDIL. We agree with Canada's argument that the USDOC's approach of characterizing reimbursement by a government to an entity for performance of certain obligations as a grant will effectively mean that the government cannot delegate any responsibility to that entity without any compensation provided in exchange for that delegation being considered a subsidy."⁷⁵

51. The Panel considered that these two obligations operated in tandem as part of the same transaction even if there was a "temporal separation" between their operation:

"[B]oth the legislation and the FMA, which impose on JDIL the obligation to perform silviculture and forest management as a condition to access timber, also impose the obligation on New Brunswick to reimburse JDIL for the performance of those obligations. We consider this to indicate that, notwithstanding the temporal separation between the imposition of the relevant silviculture and forest management obligations and the application for and receipt of the reimbursement by JDIL, the two were reciprocal considerations made in the same transaction. We note that even though the reciprocal obligations agreed to between JDIL and New Brunswick were implemented at different points of time, they were agreed to at the same time, and as part of the same transaction."⁷⁶

52. The Panel also considered that the USDOC did not adequately explain its assertion that the company at issue was allocated, as a possible "grant" under Article 1.1(a)(1)(i), rights to any additional timber generated due to its performance of the above-mentioned silviculture and forest management obligations:

"We note in this regard that JDIL's FMA with New Brunswick indicates that JDIL could be allocated additional timber generated due to silviculture activities. We consider that having an additional supply of timber, even upon payment of stumpage charges, could be commercially beneficial for a company. Thus, JDIL could potentially benefit from productivity increases resulting from its silviculture and forest management activities in the form of having access to increased supply of timber, and hence has an incentive to carry out silviculture even without reimbursements from New Brunswick. While the

⁷⁴ Panel Report, *US – Softwood Lumber VII*, para. 7.618.

⁷⁵ Panel Report, *US – Softwood Lumber VII*, para. 7.621.

⁷⁶ Panel Report, *US – Softwood Lumber VII*, para. 7.622.

USDOC did refer to one of the provisions in JDIL's FMA that indicate that JDIL could be allocated rights to any additional timber that is produced due to silviculture, we consider that the USDOC's assertion was nevertheless inadequately reasoned. This is because the USDOC did not engage with the possibility that the costs that JDIL would incur in performing silviculture and forest management activities without any reimbursement from New Brunswick may exceed any commercial advantage in the form of increased supply that may result from silviculture and forest management, due to which it may not be commercially logical for JDIL to undertake silviculture and forest management without reimbursement."⁷⁷

1.3.3.3 "potential direct transfers of funds"

53. In *Brazil – Aircraft*, the Panel had found that "a 'potential direct transfer of funds' exists only where the action in question gives rise to a benefit and thus confers a subsidy irrespective of whether any payment occurs", and that "the existence of a 'potential direct transfer of funds' does not depend upon the probability that a payment will subsequently occur".⁷⁸ The Appellate Body considered that the Panel did not have to determine whether the export subsidies at issue constituted a "direct transfer of funds" or a "potential direct transfer of funds" within the meaning of Article 1.1(a)(i) in that case, and declared the Panel findings on this point to be moot.⁷⁹

54. The Panel in *Brazil – Aircraft* rejected the argument that a subsidy exists only when the transfer of funds has actually been effectuated:

"[A]ccording to Article 1:1(i) a subsidy exists if a government practice involves a direct transfer of funds or a potential direct transfer of funds and not only when a government actually effectuates such a transfer or potential transfer (otherwise the text of (i) would read: 'a government directly transfers funds ... or engages in potential direct transfers of funds or liabilities') ... As soon as there is such a practice, a subsidy exists, and the question whether the practice involves a direct transfer of funds or a potential direct transfer of funds is not relevant to the existence of a subsidy. One or the other is sufficient. If subsidies were deemed to exist only once a direct or potential direct transfer of funds had actually been effectuated, the Agreement would be rendered totally ineffective and even the typical WTO remedy (i.e. the cessation of the violation) would not be possible."⁸⁰

55. In *EC and certain member States – Large Civil Aircraft*, the Panel set forth the following interpretation of the concept of a "potential direct transfer of funds":

"The explicit identification of 'loan guarantees' as an example of 'potential direct transfers of funds or liabilities' is instructive for the purpose of understanding the types of measures that may constitute 'potential direct transfers of funds or liabilities'. A loan guarantee may be described as a legally binding promise to repay the outstanding balance of a loan when the loan recipient defaults on its repayments. Thus, it is the promise to repay an outstanding loan in the event of default that is the financial contribution (*i.e.*, the potential direct transfer of funds), not the funds that may be transferred in the future in the event of default.

...

In our view, the fact that a loan guarantee will confer a benefit on a recipient when it enables that recipient to obtain the guaranteed loan at a below market price implies that the benefit of a potential direct transfer of funds arises from the *mere existence* of an obligation to make a direct transfer of funds in the event of default. Thus, when assessing whether a transaction involves a 'potential direct transfer[] of funds', the focus should be on the existence of a government practice that involves an obligation to make a direct transfer of funds which, *in and of itself*, is claimed and capable of conferring a benefit on the recipient that is separate and independent from the benefit

⁷⁷ Panel Report, *US – Softwood Lumber VII*, para. 7.623.

⁷⁸ Panel Report, *Brazil – Aircraft*, paras. 7.68 and 7.70.

⁷⁹ Appellate Body Report, *Brazil – Aircraft*, para. 157.

⁸⁰ Panel Report, *Brazil – Aircraft*, para. 7.13.

that might be conferred from any future transfer of funds. This can be contrasted with financial contributions in the form of direct transfers of funds, which will result in a benefit being conferred on a recipient when there is a government practice that involves a direct transfer of funds.

...

As we have previously explained, the explicit identification of 'loan guarantees' as an example of a 'potential direct transfers of funds or liabilities' is instructive for the purpose of understanding the types of measures that may constitute 'potential direct transfers of funds or liabilities'. A loan guarantee may be described as a legally binding promise to repay the outstanding balance of a loan when the loan recipient defaults on its repayments. Thus, it is the promise to repay an outstanding loan in the event of default that is the financial contribution (*i.e.*, the potential direct transfer of funds), not the funds that may be transferred in the future in the event of default."⁸¹

56. On this basis, the Panel in *EC and certain member States – Large Civil Aircraft* found that one of the challenged measures constituted a potential direct transfer of funds:

"In respect of the funding that was committed, but not disbursed under LuFo III as of 1 July 2005, the European Communities' principal argument in response to the United States' claims amounts to the submission that a government commitment of funds, without any actual disbursement of those funds, cannot amount to a 'financial contribution'. However, as we have noted elsewhere in this Report, a commitment to provide funds may well be a 'financial contribution' if in the form of a 'potential direct transfer of funds'. We understand it, the United States argues that the funds that were committed but not disbursed to Airbus under the LuFo III programme represent precisely this form of 'financial contribution'. We agree. Just as the disbursement of funds is a 'direct transfer of funds', a commitment – or a promise – to disburse funds may be properly characterized as a 'potential direct transfer of funds' falling within the definition of a 'financial contribution' set out in Article 1.1(a)(1)(i) of the SCM Agreement. Thus, on the basis of the parties' submissions and the evidence that has been presented, we find that as of 1 July 2005, the German Federal government provided Airbus with a 'potential direct transfer of funds' in the form of a commitment to transfer approximately EUR [***] to Airbus under the LuFo III programme."⁸²

57. The Panel in *US – Large Civil Aircraft (2nd complaint)* also considered the meaning of "potential direct transfer of funds". The principal point of contention between the parties was whether a "potential direct transfer of funds" can only exist when a direct transfer of funds is required upon the occurrence of a "triggering event" or condition, or whether it can be found to exist where a potential direct transfer of funds is one of a number of possible consequences following the fulfilment of a pre-defined condition. The Panel considered that the "mere possibility that a government may transfer funds" upon the fulfilment of a pre-defined condition will not be enough to satisfy the definition of a financial contribution:

"In this regard, we note that the definition of 'potential' is '*possible*' as opposed to actual, capable of coming into being or action; latent'. On its face, this definition does not appear to exclude from the reach of Article 1.1(a)(1)(i) of the SCM Agreement the possible transfer of funds identified by the European Communities. However, accepting the European Communities' submissions on this issue would require a broad interpretation of potential direct transfer of funds. The European Communities' position is essentially that any time there is a possibility that the government will transfer funds in the future, upon the occurrence of a defined triggering event, this is a financial contribution. The contextual guidance provided by the example of a 'potential direct transfer' in Article 1.1(a)(1)(i), namely a loan guarantee, suggests that this was not intended to be the case. A loan guarantee is a *commitment* by the government to assume responsibility for a loan when a defined set of circumstances arise. Therefore, the example chosen in Article 1.1(a)(1)(i) suggests that the mere

⁸¹ Panel Report, *EC and certain member States – Large Civil Aircraft*, paras. 7.302, 7.304.

⁸² Panel Report, *EC and certain member States – Large Civil Aircraft*, para. 7.1495.

possibility that a government may transfer funds upon the fulfilment of a pre-defined condition will not be enough to satisfy the definition of a financial contribution. In our view, a potential direct transfer of funds is a 'possibility' due to uncertainty about whether the triggering event will occur, rather than uncertainty about whether the transfer of funds will follow once the pre-defined event has transpired."⁸³

1.3.4 Article 1.1(a)(1)(ii): "government revenue otherwise due is foregone or not collected"

58. In *US – FSC*, the Appellate Body held that in determining if revenue "otherwise due" has been foregone, a comparison must be made between the revenue actually raised and the revenue that would have been raised "otherwise". The Panel and the Appellate Body agreed that the basis of comparison in determining what would otherwise have been due "must be the tax rules applied by the Member in question".⁸⁴

59. In *US – FSC*, the Panel applied a "but for" test in determining whether revenue had been foregone that was "otherwise due". This involved examining the situation that would have existed but for the measure in question and determining whether there would have been a higher tax liability in the absence of the measure.⁸⁵ In *US – FSC*, the Appellate Body expressed some reservations about whether the "but for" test is an appropriate general test that should apply in all situations.⁸⁶ The Appellate Body reasoned:

"[T]he word 'foregone' suggests that the government has given up an entitlement to raise revenue that it could otherwise have raised. This cannot, however, be an entitlement in the abstract, because governments, in theory, could tax *all* revenues. There must, therefore, be some defined normative benchmark against which a comparison can be made between the revenue actually raised and the revenue that would have been raised 'otherwise'...

The Panel found that the term 'otherwise due' establishes a 'but for' test in terms of which the appropriate basis of comparison for determining whether revenues are 'otherwise due' is 'the situation that would prevail but for the measures in question'. In the present case, this legal standard provides a sound basis for comparison because it is not difficult to establish in what way the ... income ... would be taxed 'but for' the contested measure. However, we have certain abiding reservations about applying any legal standard, such as this 'but for' test, in the place of the actual treaty language ... It would, we believe, not be difficult to circumvent such a test ... We observe, therefore, that, although the Panel's 'but for' test works in this case, it may not work in other cases."⁸⁷

60. In *US – FSC (Article 21.5 – EC)*, the Appellate Body clarified that there may be situations where it is possible to apply a "but for" test, namely where the measure at issue is an "exception" to a "general" rule of taxation.⁸⁸ However, a panel is not always required to identify the "general" rule of taxation. In many situations, it may be difficult to do so.⁸⁹ In such circumstances:

"Panels should seek to compare the fiscal treatment of legitimately comparable income to determine whether the contested measure involves the foregoing of revenue which is 'otherwise due', in relation to the income in question.

...

⁸³ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.164.

⁸⁴ Appellate Body Report, *US – FSC*, para. 90.

⁸⁵ Panel Report, *US – FSC*, para. 7.45.

⁸⁶ Appellate Body Report, *US – FSC*, para. 91.

⁸⁷ Appellate Body Report, *US – FSC*, paras. 90-91.

⁸⁸ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 91.

⁸⁹ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 91.

[T]he normative benchmark for determining whether revenue foregone is otherwise due must allow a comparison of the fiscal treatment of comparable income, in the hands of taxpayers in similar situations."⁹⁰

61. In *Canada – Autos*, the Appellate Body found a foregoing of revenue "otherwise due" by comparing Canada's "normal MFN duty rate" for imports of motor vehicles with the import duty exemption at issue in that case:

"We note, once more, that Canada has established a normal MFN duty rate for imports of motor vehicles of 6.1 per cent. Absent the import duty exemption, this duty would be paid on imports of motor vehicles. Thus, through the measure in dispute, the Government of Canada has, in the words of *United States – FSC*, 'given up an entitlement to raise revenue that it could 'otherwise' have raised.' More specifically, through the import duty exemption, Canada has ignored the 'defined, normative benchmark' that it established for itself for import duties on motor vehicles under its normal MFN rate and, in so doing, has foregone 'government revenue that is otherwise due'."⁹¹

62. The measure at issue in *Canada – Autos* consisted of the exemption of import duties for motor vehicles imported into Canada by Canadian car manufacturers who fulfilled certain conditions. The Appellate Body rejected the argument that the Canadian measure was "'analogous' to the situation described in footnote 1".⁹² The Appellate Body stated: "Footnote 1 ... deals with duty and tax exemptions or remissions for *exported* products. The measure at issue applies, in contrast, to *imports* ... For this reason, we do not consider that footnote 1 bears upon the import duty exemption at issue in this case."⁹³

63. In *US – Large Civil Aircraft (2nd complaint)*, the Panel found that certain measures involved a foregoing of revenue otherwise due within the meaning of Article 1.1(a)(1)(ii). The Panel recalled the Appellate Body's guidance in *US – FSC* and *US – FSC (Article 21.5 – EC)*, which it summarized as follows:

"Therefore, the Appellate Body's analysis suggests that where it is possible to identify a general rule of taxation applied by the Member in question, a 'but for' test can be applied. In other situations, the challenged taxation measure should be compared to the treatment applied to comparable income, for taxpayers in comparable circumstances in the jurisdiction in issue."⁹⁴

64. The Panel in *US – Large Civil Aircraft (2nd complaint)* then found that "[a]pplying the guidance from the Appellate Body to the *Washington B&O tax reduction*, a review of the evidence before the Panel reveals that there is indeed a general rate of taxation applicable to manufacturing activities in the State of Washington and that the tax reduction provided to aircraft manufacturing activities constitutes an exception to this rule".⁹⁵ The Panel explained that:

"In these circumstances, where it is not difficult to identify a general rule of taxation and exceptions to it, the guidance provided by the Appellate Body suggests that a 'but for' test can be applied. The relevant question is whether, 'but for' the challenged tax reduction, a higher B&O tax rate would otherwise apply to manufacturers of commercial aircraft and their components. The answer to this question is in the affirmative. The standard rate for manufacturing and wholesaling activities is 0.484 per cent and for retailing activities is 0.471 per cent. Were it not for the 'preferential rate' introduced by HB 2294, aircraft manufacturers would be subject to the rates of 0.484 per cent for manufacturing and wholesaling and 0.471 per cent for retail sales. For these reasons, the Panel finds that the reductions in the B&O tax rates constitute

⁹⁰ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 91 and 98.

⁹¹ Appellate Body Report, *Canada – Autos*, para. 91.

⁹² Appellate Body Report, *Canada – Autos*, para. 92.

⁹³ Appellate Body Report, *Canada – Autos*, para. 92.

⁹⁴ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.120.

⁹⁵ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.121.

the foregoing of revenue otherwise due and, as a result, are a financial contribution under Article 1.1(a)(1)(ii) of the SCM Agreement."⁹⁶

65. In *EU – PET (Pakistan)*, the Appellate Body noted that the "comparison under Article 1.1(a)(1)(ii) should be between the rules of taxation applied by the Member concerned to the alleged subsidy recipients, on the one hand and the rules of taxation applied by the same Member to comparably situated taxpayers that are not recipients of the alleged subsidy, on the other hand."⁹⁷ After recognizing that governments generate revenues through the imposition of duties or taxes, the Appellate Body noted that the "exemption from, or the remission of these duties or taxes, such as those referred to in paragraphs (g), (h) and (i) of Annex I of the SCM Agreement, may be found to meet the definition of government revenue foregone in Article 1.1(a)(1)(ii) of the SCM Agreement."⁹⁸

66. The Appellate Body in *Brazil – Taxation* analysed whether the Panel had erred in the determination of the benchmark treatment under Article 1.1(a)(1)(ii) by seeking "to ascertain the existence of a 'general rule of taxation' instead of examining the organizing principles and structure of Brazil's taxation regime and identifying what constitutes comparable income of comparably situated taxpayers".⁹⁹ The Appellate Body confirmed the approach followed in *US – Large Civil Aircraft (2nd complaint)* for claims under Article 1.1(a)(1)(ii), and highlighted the importance of identifying the tax treatment of comparable income of comparably situated taxpayers, and cautioned panels against artificially creating a rule and an exception where no such distinction exists.¹⁰⁰ The Appellate Body concluded:

"[I]n determining a benchmark for comparison, a panel must be cognizant of the limitations inherent in seeking to identify a general rule of taxation and an exception from that rule, because such an approach may lead to an overly narrow conception of which rules are relevant in identifying a benchmark. It is not sufficient, once a general rule of taxation has been identified, to conduct an analysis limited to the determination that, but for the challenged measure, a higher tax liability would have attached by virtue of a general rule. Rather, even if scrutiny of a Member's tax regime indicates the presence of a general rule and an exception relationship, a panel would be expected 'to further examine the structure of the domestic tax regime and its organising principles' in order to determine what is 'the tax treatment of comparable income of comparably situated taxpayers'. The Panel commenced its analysis with an examination of Brazil's domestic tax regime by identifying categories of companies subject to tax suspensions. The Panel determined, in this respect, that there were other companies, in addition to those qualified as predominantly exporting companies, that were entitled to the relevant tax suspensions. Having done so, however, the Panel ultimately limited its analysis to seeking to identify the existence of a general rule of taxation to which the challenged treatment would be an exception. By doing so, the Panel effectively predetermined a finding of the existence of the revenue otherwise due that is foregone or not collected under Article 1.1(a)(1)(ii) of the SCM Agreement.

In our view, instead of seeking to determine the existence of a general rule whereby the tax suspensions would only apply to companies structurally accumulating credits, the Panel should have determined the tax treatment of comparably situated taxpayers."¹⁰¹

67. In *Brazil – Taxation*, when assessing the Panel's comparison of the benchmark treatment and the challenged treatment, the Appellate Body rejected Brazil's argument that "the Panel should have undertaken a comparison akin to the assessment of less favourable treatment under Article III:4 of the GATT 1994":

⁹⁶ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.133. The Panel also considered a number of other measures under Article 1.1(a)(1)(ii). See Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.310-7.39, 7.504-7.514, 7.522-7.546, and 7.706-7.711.

⁹⁷ Appellate Body Report, *EU – PET (Pakistan)*, para. 5.96 (referring to Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 808 and 812).

⁹⁸ Appellate Body Report, *EU – PET (Pakistan)*, para. 5.97.

⁹⁹ Appellate Body Report, *Brazil – Taxation*, para. 5.160.

¹⁰⁰ Appellate Body Report, *Brazil – Taxation*, paras. 5.162-5.163.

¹⁰¹ Appellate Body Report, *Brazil – Taxation*, paras. 5.167-5.168.

"We do not see how this legal test, used for determining less favourable treatment under Article III:4 of the GATT 1994, could be transplanted into the analysis under Article 1.1(a)(1)(ii) of the SCM Agreement. We recall that, under Article III:4 of the GATT 1994, the less favourable treatment must affect the group of imported products, as compared to the group of like domestic products. There is an inconsistency under Article III:4 only if imported products from the complaining Member, as a group, are treated less favourably than the group of like domestic products.

By contrast, a subsidy is always conferred upon certain recipients. The Appellate Body has observed that, in determining the existence of the revenue otherwise due that is foregone under Article 1.1(a)(1)(ii), 'like will be compared with like', and that it is important to ensure that the examination under Article 1.1(a)(1)(ii) 'involves a comparison of the fiscal treatment of the relevant income for taxpayers in comparable situations'. Thus, to determine whether the revenue that is otherwise due is foregone, the challenged treatment must be compared to an objectively identifiable benchmark. This does not presuppose, however, that such a comparison should necessarily be made between the group of the entities that allegedly benefits from a subsidy, on the one hand, and the group of *all* the other entities, on the other hand. Accordingly, even if not all taxpayers in the benchmark group are paying the full amount of the relevant tax, this would not necessarily mean that there is no revenue foregone with respect to the taxpayers benefiting from a subsidy.

Thus, while both the analysis of less favourable treatment under Article III:4 and the examination under Article 1.1(a)(1)(ii) involve comparisons, this does not mean that the same analytical framework that applies to the examination of less favourable treatment under Article III:4 of the GATT 1994 is also applicable *mutatis mutandis* to the comparison of the benchmark tax treatment and the challenged tax treatment for purposes of determining whether revenue foregone under Article 1.1(a)(1)(ii) of the SCM Agreement exists."¹⁰²

68. The Appellate Body in *Brazil – Taxation* found that in ascertaining whether there is a financial contribution in the form of "government revenue that is otherwise due" being foregone or not collected, consideration should also be given to whether the government collects the revenue at the time foreseen in the relevant regulations:

"A government foregoes or does not collect the 'revenue that is otherwise due' in a situation where it gives up or relinquishes its entitlement to collect revenue that is owed or payable in other circumstances. In the present dispute, when the tax exemptions and reductions apply, the Brazilian Government does not collect in full the tax revenue when it normally would, or collects it in part. The fact that, ultimately, the amount of the tax collected under the benchmark treatment and the challenged treatment may nominally be the same does not detract from the fact that, under the benchmark treatment, in the scenario when non-accredited companies are unable to offset their credits immediately, the Brazilian Government would collect and retain, for a certain period, the amount of tax payable to it. During this period of time, the Brazilian Government can enjoy the cash available to it and earn interest on it. By contrast, when tax exemptions and reductions are applied, the Brazilian Government collects the tax later in time and does not enjoy the availability of cash as it otherwise would under the benchmark treatment. Thus, under the challenged treatment, the Brazilian Government would not collect the tax at the time it normally would under the benchmark treatment. By doing so, in our view, the Brazilian Government would not collect the revenue that would be otherwise due to it.

Accordingly, in the scenario where the buyer is unable to offset the credit during the same taxation period, the non-collection of the tax revenue by the Brazilian Government at the time when it normally would do so amounts to 'government revenue that is otherwise due' being 'foregone or not collected' within the meaning of Article 1.1(a)(1)(ii) of the SCM Agreement."¹⁰³

69. The Appellate Body in *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU) found that the Panel had erred in focusing on Boeing's use of the FSC/ETI concessions in determining whether

¹⁰² Appellate Body Report, *Brazil – Taxation*, paras. 5.208 – 5.210.

¹⁰³ Appellate Body Report, *Brazil – Taxation*, paras. 5.220-5.221.

the United States continued to provide a financial contribution in the form of revenue foregone, and that the focus should have been on "whether a government has given up its entitlement to revenue, instead of whether the available tax concessions were used by the eligible taxpayers".¹⁰⁴

70. The Panel in *US – Softwood Lumber VII* considered that, in determining whether revenue has been foregone by a government or a public body, an investigating authority must compare the revenue actually raised by a government or "public body" to the revenue that it otherwise would have raised, in the light of the tax or fiscal rules operating in the jurisdiction at issue:

"Article 1.1(a)(1) is concerned with the different forms that a 'financial contribution' may take. Under Article 1.1(a)(1)(ii), a financial contribution may take a form of foregoing government revenue that is otherwise due or not collected. The Appellate Body has stated that a situation where a government foregoes or does not collect its revenue that is 'otherwise due' implies that less revenue has been raised by the government than would have been raised in a different situation. In other words, a government 'gives up or relinquishes its entitlement to collect revenue that is owed or payable in other circumstances'. In determining if revenue 'otherwise due' has been foregone, a comparison must be made between the revenue actually raised and the revenue that would have been raised 'otherwise'. The basis of such a comparison is normally the tax or fiscal rules in the jurisdiction at issue."¹⁰⁵

71. The Panel in *US – Softwood Lumber VII* considered that the USDOC had incorrectly characterized, as "revenue foregone" under Article 1.1(a)(1)(ii), a credit issued by a state-owned supplier of electricity (NB Power) to a company in exchange for the state-owned supplier's purchase of renewable electricity from that company. The Panel considered, *inter alia*, that the credit amount "does not constitute an amount that would be otherwise due to NB Power"¹⁰⁶, as the credit is derived from revenue generated from the sale of the renewable electricity to the company:

"NB Power generates revenue by selling electricity to customers in New Brunswick, including the Irving Group. Therefore, any amount that is due to NB Power is, ultimately, in exchange for the provision of electricity to consumers in New Brunswick. Under the [large industrial renewable energy purchase programme (LIREPP)], NB Power pays for the renewable electricity it purchases pursuant to the programme from the eligible companies in the Irving Group by issuing a credit on Irving Paper's electricity bills. We consider that the LIREPP credit is a payment mechanism under the LIREPP Agreement between NB Power and the Irving Group, and represents an amount that NB Power owes to the Irving Group in return for the purchase of renewable electricity. Although the credit amount ultimately reduces the Irving Group's electricity bills, it does not constitute an amount that would be otherwise due to NB Power. This is not an amount that would otherwise have accrued to NB Power, since NB Power would, in any event, have had to pay that amount to Irving Paper in return for the renewable electricity that it purchased from eligible companies in the Irving Group. The USDOC acknowledged that, 'the program does encompass, in part, the purchase of a good or service'. However, it is the revenue generated from these 'purchases' of electricity that is used as a credit on Irving Paper's bill against the Irving Group's overall electricity charges. As such, we consider that the USDOC's finding that the LIREPP credits are revenue foregone and therefore the amount of the countervailable benefit is not one that an unbiased and objective investigating authority could have reached."¹⁰⁷

72. The Panel also considered that the credit provided by NB Power was, at least in part, a function of the purchase of a requisite amount of renewable electricity specified in the LIREPP Agreement, and that the amount of the electricity was thus not "immaterial" to the provision of the credit:

¹⁰⁴ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU), para. 5.160.

¹⁰⁵ Panel Report, *US – Softwood Lumber VII*, para. 7.690.

¹⁰⁶ Panel Report, *US – Softwood Lumber VII*, para. 7.703.

¹⁰⁷ Panel Report, *US – Softwood Lumber VII*, para. 7.703.

"We understand that the credit is determined in connection with the Target Reduction Percent, which is the percentage by which qualifying companies in New Brunswick would have to reduce their electricity costs to be in line with the average cost of electricity in provinces where those companies' competitors are located. While the Target Reduction Percent may be set in accordance with the LIREPP policy objectives, it does not follow that the amount of electricity purchased is *immaterial* to the credit for the purposes of characterizing the financial contribution pursuant to Article 1.1(a)(1). To the contrary, it is a precondition to the Irving Group receiving the credit that NB Power purchases the requisite amount of electricity. Both the design *and* operation of the LIREPP are relevant considerations in determining its proper characterization for the purpose of Article 1.1(a)(1). We consider that by focusing on the design of the programme, i.e. that the credit was, according to the United States, predetermined in order to meet certain policy objectives, the USDOC failed to give relevant consideration to the operation of the programme. Specifically, the USDOC failed to consider that the requisite amount of electricity must, as a matter of fact, be purchased by NB Power before a credit is issued to the Irving Group. We find that this is not a conclusion that an unbiased and objective investigating authority could have reached."¹⁰⁸

73. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel considered "government revenue forgone" as the functional equivalent of a "direct transfer of funds":

"The Panel recalls that the purpose of selecting a normative benchmark is to determine, through a comparison with the challenged tax treatment, whether 'government revenue that is otherwise due is foregone or not collected' within the meaning of Article 1.1(a)(1)(ii). The Panel notes as well that the first category of financial contributions provided for under Article 1.1(a)(1)(i) includes various direct transfers of funds or potential direct transfers of funds. This provides some context for understanding the inclusion of the second category, which is the one relevant in this case. The Panel considers that where government revenue is otherwise due and the government foregoes or does not collect the amount otherwise due, this is the functional equivalent of a direct transfer of funds from the government."¹⁰⁹

74. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel stated that under Article 1.1(a)(1)(ii), the inquiry is not whether similar products are taxed similarly:

"The Panel understands that in Malaysia's view qualifying biofuels and palm oil-based biofuel should be considered as similarly situated by the tax regime and should, therefore, receive similar tax treatment. Accordingly, the favourable treatment of qualifying biofuels as compared to palm oil-based biofuel should be considered as a financial contribution within the meaning of Article 1.1(a)(1)(ii). The Panel considers, however, that products that are similar (or like or even identical) from the perspective of product characteristics, uses, substitutability, production methods, tariff classifications, etc., are not necessarily similarly situated from the perspective of a Member's tax regime and tax principles. At this stage of the analysis, the Panel must focus on whether the allegedly subsidized taxpayer receives from the government the functional equivalent of a direct transfer of funds in the form of an amount of taxes that were due otherwise but was not required to be paid. Accordingly, the question for the Panel is not whether similar products are taxed similarly, but rather whether the challenged tax treatment constitutes the kind of departure from that tax regime and tax principles such that government revenue that was otherwise due was foregone or not collected."¹¹⁰

75. Similarly, the Panel in *EU and Certain Member States – Palm Oil (Malaysia)* stated that in a corporate tax regime which entails variations in the generally applicable tax rate depending on the size or other characteristics of companies, the tax rate applicable to a particular group of companies may not be treated as the normative benchmark in assessing, under Article 1.1(a)(1)(ii), the treatment provided to another group of companies:

¹⁰⁸ Panel Report, *US – Softwood Lumber VII*, para. 7.704.

¹⁰⁹ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, para. 7.1337.

¹¹⁰ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, para. 7.1311.

"In this context, the Panel considers that 'comparability' and 'similarly situated' are not determined in the abstract, nor on the basis of what is considered legitimate, appropriate or fair. Rather, 'comparability' and 'similarly situated' are determined in relation to the 'structure of the domestic tax regime and its organising principles.' The concern of the Appellate Body in *Brazil – Taxation* was over-reliance on the fact that the challenged measure took the form of an exception to a general rule. When a general rule appears to be broadly applicable and subject to various exceptions, it may be necessary to look further to examine the extent to which the general rule, in light of the other exceptions, constitutes an inadequate benchmark because it insufficiently represents the structure of the tax regime and its organizing principles. This can be understood by considering, as the Appellate Body did in *Brazil – Taxation*, an example of a generally applicable tax with numerous and various exceptions. Thus, a corporate tax rate that is in principle applicable to all commercial entities, but with numerous and overlapping adjustments for various categories, sizes and circumstances of the entities taxed could not serve as an adequate benchmark for any one of the exceptions because it could be that few if any entities actually pay the tax at the generally applicable rate. This means that the tax regime and its organizing principles that determine the normative benchmark may be found in rules that take the form of exceptions to a general rule as much as in the form of the general rules themselves.

This notion may be further illuminated with an example of a tax regime where the tax rate depends on the size of the company. If the tax rate increased according to the size, then small companies might appear to pay less than is otherwise due. If the tax rate decreases according to size, then large companies might appear to pay less than is otherwise due. If, however, company size is understood to be the organizing principle of the tax regime, then small, medium and large companies would not be considered as similarly situated and the amounts paid by companies of other sizes would not be relevant to determining what amount of tax is otherwise due. It might be observed that all sizes are not available to all companies and this might justify additional scrutiny of the breakdown of size categories and differences in tax rates, *et cetera*, possibly concluding nevertheless that company size is indeed an organizing principle of the tax regime."¹¹¹

76. In *EU and Certain Member States – Palm Oil (Malaysia)*, the challenged measure was a tax scheme under which the amount of the tax was determined based on the energy content of the fuel sold in France:

"[E]ntities that release fuel for consumption within the territory of France are liable to pay the TIRIB as an additional tax that varies in relation to the extent to which the energy content of the fuel released achieves established incorporation targets for qualifying energy sources. The Panel recalls that the TIRIB is applied in addition to the value added tax (VAT) and the internal consumption tax on energy products (TICPE). The amount of the TIRIB is determined according to the TIRIB formula.

he TIRIB formula results in a tax rate that varies in direct proportion to the factor (IT% - AI%), which is the difference between the targeted energy incorporation of qualifying biofuel and the actual incorporation of qualifying biofuel."¹¹²

77. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel declined to treat the fact that no tax is due if the fuel sold satisfies the prescribed content requirements, as the normative benchmark for purposes of its assessment under Article 1.1(a)(1)(ii):

"The Panel understands that all potential taxpayers operate under a scheme under which no amount of tax is due if the fuel they release satisfies the incorporation targets. Access to the zero tax treatment is otherwise uninhibited for these taxpayers. While it is established that some amount of tax was collected pursuant to the French TIRIB during the time periods for which the Panel has information, the extent of any failure of fuels released for consumption in France to satisfy the incorporation targets

¹¹¹ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1339-7.1340.

¹¹² Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1313-7.1314.

is extremely small. Nevertheless, the Panel considers that under Article 1.1(a)(1)(ii), the issue is not whether the French TIRIB is a behavioural tax or has an environmental purpose or was intended to raise revenue. The extent to which these features constitute elements of the challenged tax treatment and/or elements of the tax regime and tax principles that will define the normative benchmark does not require the Panel to assess the legitimacy of these features as elements of a Member's tax rules.

The Panel considers that the key concept guiding the selection of an appropriate normative benchmark derives from the term otherwise due in the text of Article 1.1(a)(1)(ii). In particular, the appropriate normative benchmark represents the treatment associated with the tax liability otherwise due in accordance with the structure of the domestic tax regime and its organising principles as adopted by the Member pursuant to its own authority in comparison to the challenged tax treatment. The Panel is not persuaded that the collection of no amount of tax pursuant to the French TIRIB constitutes the appropriate normative benchmark treatment. Under certain circumstances under the French TIRIB an amount of tax liability is imposed on the taxpayer and, when paid, this amount represents government revenue that is due. The Panel does not consider that it would be appropriate to find under such a scheme that the structure of the domestic tax regime and its organising principles imposes no tax liability as a normative benchmark regardless of the frequency or the infrequency with which the circumstances associated with no tax liability arise. Instead, the appropriate normative benchmark should take into account those circumstances in which a tax liability arises in accordance with the 'structure of the domestic tax regime and its organising principles'.

...

For the above reasons, the Panel finds that the collection of no amount of tax pursuant to the French TIRIB is not an appropriate normative benchmark in this case."¹¹³

78. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel considered the formula used to determine the amount of the tax depending on the contents of the fuel sold, as the most appropriate normative benchmark for purposes of Article 1.1(a)(1)(ii). On this basis, the Panel concluded that the challenged measure did not entail government revenue forgone and therefore no financial contribution:

"In weighing the appropriateness of these two possible normative benchmarks, the Panel considers that the design and operation of the French TIRIB, as well as how it is situated in relationship to the broader tax regime, reveal that the fact that the amount of tax due varies in direct proportion to the factor (IT% - AI%) is a central and essential organizing principle of the French TIRIB. Thus, the Panel considers that this element is not an element of the TIRIB formula amenable to be disregarded as a principle of taxation under this scheme. As such, the Panel finds that the elements of the TIRIB formula go hand in hand and do not exist in isolation, and are accurately described as being inseparably linked as integral parts of the TIRIB formula. In establishing a formula to determine the rate of tax that is proportional to the factor (IT% - AI%), the design of the French TIRIB establishes a range of tax rates each of which is applicable to similarly situated taxpayers. The Panel considers that for all taxpayers to which the TIRIB formula applies, the amount of tax that is due is determined by the formula and no other amount of tax is due. In sum, whatever tax liability is imposed by the French TIRIB it represents an additional tax on operators releasing fuel for consumption in France that are similarly situated to the extent that the targeted portion of the fuel released does not incorporate qualifying biofuels. Accordingly, the Panel finds that the TIRIB formula represents the most appropriate normative benchmark for comparison with the challenged tax treatment.

...

¹¹³ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1324-7.1325 and 7.1327.

The Panel finds that the challenged tax treatment consists of the treatment of taxpayer entities releasing fuel for consumption in France that partially or fully satisfies the incorporation target for qualifying biofuel. The Panel finds that the TIRIB formula represents the most appropriate normative benchmark for comparison with the challenged tax treatment. Because the challenged tax treatment is part of and incorporated into the benchmark tax treatment, both of which flow from the application of the TIRIB formula, the challenged tax treatment and the benchmark tax treatment are the same.

Accordingly, the Panel finds that there is no difference between the challenged tax treatment and the benchmark tax treatment, and therefore, no government revenue has been foregone or not collected and no financial contribution exists within the meaning of Article 1.1(a)(1)(ii)."¹¹⁴

1.3.4.1 Footnote 1

1.3.4.1.1 General

79. The Panel in *India – Export Related Measures* stated that the second part of footnote 1 of the SCM Agreement "describes the two groups of measures that 'shall not be deemed to be a subsidy', provided they are also in accordance with the Note to Article XVI and Annexes I to III."¹¹⁵ According to the Panel, these two groups of measures are (a) "the exemption of an exported product from the duties or taxes borne by the like product when destined for domestic consumption"; and (b) "the remission of such duties or taxes in amounts not in excess of those which have accrued". The Panel considered the difference between these two groups to be that "in the case of exemptions, the duty or tax liability never arises, whereas, in the case of remissions, the liability first arises, but is later remitted, including by returning the payment if one was already made."¹¹⁶

80. On this basis, the Panel summarized the "four definitional elements" of the measures described in footnote 1 as follows: "the description of these two groups of measures in footnote 1 contains four definitional elements, namely, there must be (1) an exemption or remission (2) of duties or taxes (3) on an exported product, (4) not in excess of the duties and taxes which have accrued."¹¹⁷

81. In *India – Sugar and Sugarcane*, the Panel set out the required criteria for measures which are not deemed to be a subsidy under footnote 1 of the SCM Agreement:

"As noted, to fall under the scope of footnote 1, a measure has to be (i) a remission or drawback; (ii) of import charges; (iii) on imported inputs that are consumed in the production of the exported product; and (iv) not in excess of those levied on those inputs."¹¹⁸

82. The Panel also noted that:

"[F]ootnote 1, read in conjunction with Annex II of the SCM Agreement, requires that imported inputs be 'used in the production process' and be 'physically present in the product exported'. We agree with Australia that this is not the case under the DFIA Scheme because it provides for duty-free importation of raw sugar (i.e. the input) after the exportation of white sugar (i.e. the 'product exported'). The raw sugar imported between 1 October 2019 and 30 September 2021 is not used in the production process of, and is not physically present in, the white sugar exported between 28 March and 30 September 2018. Clearly, therefore, the remission under

¹¹⁴ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1344 and 7.1346-7.1347.

¹¹⁵ Panel Report, *India – Export Related Measures*, para. 7.168.

¹¹⁶ Panel Report, *India – Export Related Measures*, para. 7.169.

¹¹⁷ Panel Report, *India – Export Related Measures*, para. 7.170.

¹¹⁸ Panel Report, *India – Sugar and Sugarcane*, para. 7.286.

the DFIA Scheme does not apply to 'imported inputs that are consumed in the production of the exported product', as footnote 1 requires."¹¹⁹

83. On this basis, the Panel concluded that the respondent's DFIA Scheme did not fall within the scope of footnote 1 of the SCM Agreement to be deemed not a subsidy:

"India argues that 'an exporter is only entitled to claim an exemption on import duty for future imports of raw sugar to the extent of the raw sugar that was in fact consumed in the production of exported white sugar'. India also points out that 'there exists a verification mechanism to ensure that only the specific inputs actually consumed in the export[ed] product are allowed [to be imported] duty free ... under DFIA'. As noted above, in our view, to fall within the scope of footnote 1, the imported inputs that benefit from the remission must be consumed in the production of the exported product, which is not the case under the DFIA Scheme. As long as this important requirement is not met, it is immaterial, in our view, whether the quantity of inputs imported duty free subsequent to the exportation of the final product corresponds to the quantity of inputs used in the production of that final product. We therefore find India's argument unconvincing.

Finally, we note India's statement that 'the DFIA can be transferred from one entity to another'. In our view, in the circumstances of this dispute, the transferability of the DFIA further underscores the disconnect between the imported inputs and the exported final product, since the importer of the inputs and the exporter of the final product may not be the same entity.

In light of the above, we conclude that India has failed to establish that the DFIA Scheme as it applies to sugar falls under the scope of footnote 1 to the SCM Agreement."¹²⁰

1.3.4.1.2 "In accordance with... the provisions of Annexes I through III"

84. In setting out the applicable legal standard under footnote 1, the Panel in *India – Export Related Measures* pointed out that the footnote must be read in accordance with Annexes I to III of the SCM Agreement.¹²¹

85. With respect to Annex I, the Panel found that:

"Annex I contains the illustrative list of export subsidies. Items (g), (h), and (i) list, as export subsidies, the exemption, remission, deferral, or drawback of certain indirect taxes and import charges on exported products, in certain defined circumstances. Because footnote 1 must be read in accordance with Annex I, a measure falling within the definition of any of items (g), (h), or (i) would not benefit from the shelter of footnote 1."¹²²

86. Turning to the facts of the dispute, the Panel in *India – Export Related Measures* found that capital goods, whose importation was exempt from customs duties under India's EOU/EHTP/BTP and EPCG Schemes, were not inputs consumed in the production of an exported product, in accordance with Annex I(i) and Annex II of the SCM Agreement.¹²³ Therefore, the Panel concluded that the exemption of these goods from customs duties under India's Schemes did not meet the conditions of footnote 1 of the SCM Agreement, read together with Annex I(i).¹²⁴

1.3.4.1.3 "Excess Remissions Principle"

87. In *EU – PET (Pakistan)*, the Appellate Body explained that "while Article 1.1(a)(1)(ii) provides a general description of revenue foregone, footnote 1, appended thereto, identifies

¹¹⁹ Panel Report, *India – Sugar and Sugarcane*, para. 7.288.

¹²⁰ Panel Report, *India – Sugar and Sugarcane*, paras. 7.289–7.291.

¹²¹ Panel Report, *India – Export Related Measures*, para. 7.171.

¹²² Panel Report, *India – Export Related Measures*, para. 7.173.

¹²³ Panel Report, *India – Export Related Measures*, paras. 7.196–7.216 and 7.243–7.247.

¹²⁴ Panel Report, *India – Export Related Measures*, paras. 7.236 and 7.247.

specific instances of revenue foregone that shall not be deemed to be subsidies. Footnote 1 deals with exemption or remission of duties or taxes on exported products."¹²⁵

88. In *EU – PET (Pakistan)*, the Panel held that in the context of duty drawback schemes, a subsidy exists only when an excess remission occurs representing government revenue foregone that is otherwise due within the meaning of Article 1.1(a)(1)(ii) and footnote 1. Referring to this as "excess remissions principle", the Panel explained that financial contribution, in the case of duty drawback schemes, is limited to the excess amount of the remission:

"Article 1.1(a)(1)(ii) is silent regarding what two things should be compared to determine whether import duty remissions obtained by a company under a duty drawback scheme like the MBS constitute revenue forgone otherwise due. Footnote 1, however, attaches to this provision, and contains crucial guidance on this score. Footnote 1 consists of one sentence with two basic parts. The first identifies legal provisions that the remainder of the sentence are '[i]n accordance with'. The second identifies two situations, i.e. (a) the 'exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption'; or (b) 'the remission of such duties or taxes in amounts not in excess of those which have accrued', that 'shall not be deemed to be a subsidy'. Attaching footnote 1, which refers to a 'subsidy', to Article 1.1(a)(1)(ii), which defines a 'financial contribution' (i.e. a part of a subsidy) in terms of revenue forgone otherwise due, indicates that it should be interpreted *vis-à-vis* that article, and is further an implicit recognition of the close relationship between the concepts of revenue forgone otherwise due and a subsidy. That is, as panels have observed, where 'financial contributions' exist in the form of revenue forgone otherwise due, a finding of a 'benefit' – and hence a 'subsidy' – readily follows.

The language 'shall not be deemed to be a subsidy' in footnote 1 indicates that, in the absence of further qualification, the two situations described are never subsidies under Article 1. Of the two, the latter appears the more material and contains the terms at which the parties direct their arguments, i.e. 'the remission of such duties or taxes in amounts not in excess of those which have accrued'. The parties appear to agree, and we see no reason to doubt, that the 'duties' that 'accrued' in this context are import duties that accrued on imported inputs consumed in the production of a subsequently exported product. Thus, the comparison under Article 1.1(a)(1)(ii) is between *remissions of duties* obtained by a company under a duty drawback scheme, on the one hand, and *duties that accrued* on imported production inputs used by that company to produce a subsequently exported product, on the other hand. A subsidy exists insofar as the former exceeds the latter, i.e. an 'excess' remission occurs representing revenue forgone otherwise due. For ease of reference, this Report refers to this as the Excess Remissions Principle."¹²⁶

89. The Panel further stated that footnote 1 and the term "in accordance with" suggest that the "Excess Remissions Principle" is in agreement with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement equally:

"The first part of footnote 1 reads: 'In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement'. The word 'accordance' means '[a]greement; conformity; harmony'. Thus, the Excess Remissions Principle is 'in agreement with', 'in conformity with' and/or 'in harmony with' the cited provisions. The footnote refers to these provisions equally, suggesting that the Excess Remissions Principle is equally in agreement with each."¹²⁷

90. The Panel in *EU – PET (Pakistan)* concluded that the "Excess Remissions Principle provides the legal standard under which to determine whether remissions of import duties obtained under a duty drawback scheme constitutes a financial contribution in the form of revenue forgone

¹²⁵ Appellate Body Report, *EU – PET (Pakistan)*, para. 5.97.

¹²⁶ Panel Report, *EU – PET (Pakistan)*, paras. 7.36-7.37.

¹²⁷ Panel Report, *EU – PET (Pakistan)*, para. 7.39.

otherwise due under Article 1.1(a)(1)(ii) of the SCM Agreement".¹²⁸ The Panel further rejected the European Union's position that Annex II and/or Annex III provides a relevant reason to depart from the Excess Remissions Principle and explained that "even if the exporting Member has no reliable system of tracking inputs consumed in the production of a relevant exported product and in the absence of a further examination by the exporting Member of that issue, investigating authorities should still determine if an excess remission occurred".¹²⁹

91. Agreeing with the Panel, the Appellate Body in *EU – PET (Pakistan)* found that "a harmonious reading of Article 1.1(a)(1)(ii), footnote 1, and Annexes I(i), II and III to the SCM Agreement and the *Ad Note* to Article XVI of the GATT 1994 confirms that duty drawback schemes can constitute an export subsidy that can be countervailed only if they result in a remission or drawback of import charges 'in excess' of those actually levied on the imported inputs that are consumed in the production of the exported product. Thus, in the context of duty drawback schemes, the financial contribution element of the subsidy (i.e. the government revenue foregone that is otherwise due) is limited to the excess remission or drawback of import charges and does not encompass the entire amount of the remission or drawback of import charges."¹³⁰

92. The Appellate Body in *EU – PET (Pakistan)* confirmed the Panel's findings that "any perceived silence connected to the procedural step in Annex II(II)(2) 'does not mean that other portions of Annex II cease to speak and [the Panel] recall[ed] that the entirety of Annex II(II)(2) only operates in the presence of an allegation that a 'drawback scheme [...] conveys a subsidy by reason of over-rebate or excess drawback'".¹³¹ The Appellate Body clarified that:

"The perceived silence in Annex II and III to the SCM Agreement, referred to by the European Union, is not one that pertains to the definition of the subsidy, and in particular to what constitutes the financial contribution element of the subsidy, in the form of government revenue foregone. Instead the 'perceived silence' relates to a procedural step in the context of an investigating authority's inquiry into whether the excess remission or drawback of import charges occurred. As regards this procedural step, where an investigating authority determines that there is no verification system in place in the exporting Member, or a verification system is in place but it is not fit for purpose, or it has not been applied effectively by the exporting Member, and where a further examination by the exporting Member has not been undertaken or is considered unsatisfactory by the investigating authority, it is true that Annexes II and III do not explicitly provide for what should happen next. Nonetheless, the SCM Agreement, as a whole, is not silent, and the perceived 'silence' in Annexes II and III does not grant an investigating authority the liberty to depart from these other disciplines of the SCM Agreement. In particular, Article 12.7 of the SCM Agreement allows an investigating authority to rely on the 'facts available' on its investigation record to complete its inquiry into whether a duty drawback scheme conveys a subsidy by reason of excess drawback of import charges on inputs."¹³²

1.3.5 Article 1.1(a)(1)(iii): a government provides goods or services other than general infrastructure, or purchases goods

1.3.5.1 General

93. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body observed that subparagraph (iii) of Article 1.1(a)(1) contemplates two distinct types of transactions: the first is where a government "provides goods or services other than general infrastructure"; and the second relates to situations in which a government "purchases goods" from an enterprise.¹³³

94. In *US – Softwood Lumber IV*, the Appellate Body, after noting that "[a]n evaluation of the existence of a financial contribution involves consideration of the nature of the transaction through

¹²⁸ Panel Report, *EU – PET (Pakistan)*, para. 7.56.

¹²⁹ Panel Report, *EU – PET (Pakistan)*, para. 7.56.

¹³⁰ Appellate Body Report, *EU – PET (Pakistan)*, para. 5.134.

¹³¹ Appellate Body Report, *EU – PET (Pakistan)*, para. 5.126.

¹³² Appellate Body Report, *EU – PET (Pakistan)*, para. 5.139.

¹³³ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 618.

which something of economic value is transferred by a government"¹³⁴, explained that this provision foresees two types of transaction, and made the following general remarks on the scope of Article 1(a)(1)(iii) in this regard:

"As such, the Article contemplates two distinct types of transaction. The first is where a government provides goods or services other than general infrastructure. Such transactions have the potential to lower artificially the cost of producing a product by providing, to an enterprise, inputs having a financial value. The second type of transaction falling within Article 1.1(a)(1)(iii) is where a government purchases goods from an enterprise. This type of transaction has the potential to increase artificially the revenues gained from selling the product."¹³⁵

1.3.5.2 "provides"

95. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body analysed the similarities and differences between financial contributions set forth in subparagraph (i) and the first sub-clause of subparagraph (iii) of Article 1.1(a)(1):

"In the case of the provision of goods or services, subparagraph (iii) does not specify whether the goods or services are provided gratuitously or in exchange for money or other goods or services. Thus, the provision of goods or services may include transactions in which the recipient is not required to make any form of payment, as well as transactions in which the recipient pays for the goods or services. Therefore, what is captured in the first sub-clause of subparagraph (iii), as well as in subparagraph (i), is a government's provision of goods or services, or of funds, irrespective of whether this is done gratuitously or in exchange for consideration. The difference between the two types of government conduct, however, lies in what is being transferred by the government. Under subparagraph (i), the government transfers financial resources, while under subparagraph (iii) (first sub-clause), the government provides a good or service."¹³⁶

96. In *US – Softwood Lumber IV*, the Appellate Body upheld the Panel's finding that the stumpage arrangements at issue "provide" goods within the meaning of Article 1.1(a)(1)(iii):

"[W]e begin with the ordinary meaning of the term. Before the Panel, the United States pointed to a definition of the term 'provides', which suggested that the term means, *inter alia*, to 'supply or furnish for use; make available'. This definition is the same as that relied upon by USDOC in making its determination that 'regardless of whether the Provinces are supplying timber or making it available through a right of access, they are providing timber' within the meaning of the provision of United States countervailing duty law that corresponds to Article 1.1(a)(1)(iii) of the *SCM Agreement*. We note that another definition of 'provides' is 'to put at the disposal of'.

...

With respect to Canada's first argument, we do not see how the general governmental acts referred to by Canada would necessarily fall within the concept of a government 'making available' services or goods. In our view, such actions would be too remote from the concept of 'making available' or 'putting at the disposal of', which requires there to be a reasonably proximate relationship between the action of the government providing the good or service on the one hand, and the use or enjoyment of the good or service by the recipient on the other. Indeed, a government must have some control over the *availability* of a specific thing being 'made available'.

...

¹³⁴ Appellate Body Report, *US – Softwood Lumber IV*, para. 52.

¹³⁵ Appellate Body Report, *US – Softwood Lumber IV*, para. 53.

¹³⁶ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 618.

In any event, in our view, it does not make a difference, for purposes of applying the requirements of Article 1.1(a)(1)(iii) of the *SCM Agreement* to the facts of this case, if 'provides' is interpreted as 'supplies', 'makes available' or 'puts at the disposal of'.¹³⁷

97. In *US – Softwood Lumber IV*, the Appellate Body cautioned against equating the meaning of the term "provide" across different agreements:

"With respect to Canada's second argument regarding the *Agreement on Agriculture* and the GATS, the articles cited by Canada involve the provision of 'subsidies' or 'support'. We note that in Article 1.1(a)(1)(iii) of the *SCM Agreement*, the term 'provides' relates to the provision of 'goods' and 'services' in the context of describing a certain type of financial contribution. The different context of these provisions means that it is not necessarily appropriate to equate, precisely, the scope of the term 'provide' or 'provides' as they are used in these different agreements."¹³⁸

98. Turning to the facts of that case, the Appellate Body explained that:

"[W]e note that the Panel found that stumpage arrangements give tenure holders a right to enter onto government lands, cut standing timber, and enjoy exclusive rights over the timber that is harvested. Like the Panel, we conclude that such arrangements represent a situation in which provincial governments provide standing timber. Thus, we disagree with Canada's submission that the granting of an intangible right to harvest standing timber cannot be equated with the act of providing that standing timber. By granting a right to harvest, the provincial governments put particular stands of timber at the disposal of timber harvesters and allow those enterprises, exclusively, to make use of those resources. Canada asserts that governments do not supply felled trees, logs, or lumber through stumpage transactions. In our view, this assertion misses the point, because felled trees, logs and lumber are all distinct from the 'standing timber' on which the Panel based its conclusions. Moreover, what matters, for purposes of determining whether a government 'provides goods' in the sense of Article 1.1(a)(1)(iii), is the consequence of the transaction. Rights over felled trees or logs crystallize as a natural and inevitable consequence of the harvesters' exercise of their harvesting rights. Indeed, as the Panel indicated, the evidence suggests that making available timber is the *raison d'être* of the stumpage arrangements. Accordingly, like the Panel, we believe that, by granting a right to harvest standing timber, governments provide that standing timber to timber harvesters. We therefore agree with the Panel that, through stumpage arrangements, the provincial governments 'provide' such goods, within the meaning of Article 1.1(a)(1)(iii) of the *SCM Agreement*."¹³⁹

99. In *EC and certain member States – Large Civil Aircraft*, the Appellate Body found that the Panel erred in its interpretation and application of Article 1.1(a)(1)(iii) by failing to recognize that the relevant transaction for purposes of its analysis under Article 1.1(a)(1)(iii) was the *provision* of goods or services in the form of infrastructure to Airbus, not the *creation* of that infrastructure.¹⁴⁰ The Appellate Body began by noting that the ordinary meaning of the verb "provide" is to "[s]upply or furnish for use; make available".¹⁴¹ The Appellate Body confirmed that "when a good or service has not been *provided* by a government, there cannot be a financial contribution cognizable under Article 1.1(a)(1)(iii)".¹⁴² However, the Appellate Body clarified that:

"While government action concerning the creation of a good or service may not be relevant if that good or service is not ultimately provided to a recipient, we do not understand on what basis such actions would necessarily be excluded in assessing what has been provided. Recalling the meaning of the term 'provide' set out above—supply or furnish for use; make available—we consider that this term permits taking into account what was involved in supplying or furnishing that infrastructure. The

¹³⁷ Appellate Body Report, *US – Softwood Lumber IV*, paras. 69, 71 and 73.

¹³⁸ Appellate Body Report, *US – Softwood Lumber IV*, para. 74.

¹³⁹ Appellate Body Report, *US – Softwood Lumber IV*, para. 75.

¹⁴⁰ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 966.

¹⁴¹ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 963.

¹⁴² Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 964.

creation of infrastructure is a precondition, and thus necessary, for the provision of that infrastructure. We therefore do not view the use of the term 'provision' in Article 1.1(a)(1)(iii) as excluding the possibility that circumstances of the creation of infrastructure may be relevant to a proper characterization of what it is that is provided."¹⁴³

100. The Panel in *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, after rejecting the European Union's argument that intellectual property rights may be considered "goods" under Article 1.1(a)(1)(iii), nonetheless addressed the European Union's argument that the United States "provides" such intellectual property goods through the challenged transactions at issue. The European Union specifically argued that "the United States 'provides' Boeing with patents and other rights on the grounds that US law and regulations generally provide contractors with the right to receive title to inventions that arise from a funding agreement with the US government'."¹⁴⁴ Accordingly, the Panel observed that the European Union's argument seemed to be "that where a law lays down the conditions under which rights to title to inventions can be obtained, the government thereby 'provides' these rights within the meaning of Article 1.1(a)(1)(iii)."¹⁴⁵ The Panel explained that this position cannot be reconciled with the Appellate Body's statements in *US – Softwood Lumber IV* and rejected the European Union's arguments:

"The Appellate Body has observed that the term 'provide' has been defined as 'supply or furnish for use; make available' and 'to put at the disposal of'.¹⁴⁶ The Appellate Body has also explained that there must be a 'reasonably proximate relationship' between the governmental action of providing the good or service and the use or enjoyment of the good or service by the recipient. It stated that 'a government must have some control over the *availability* of a specific thing being 'made available'. The European Union does not explain how its interpretation of 'provide' can encompass situations where a law merely defines the conditions under which a 'right to take title' can be acquired in the future, in the event that a patentable invention, yet to exist, is subsequently developed, and in particular does not explain how its reading is consistent with these Appellate Body pronouncements."¹⁴⁷

101. In *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, the Panel disagreed with the underlying logic of the European Union's argument that, where a government makes a financial contribution for the purpose of supporting a firm's financing of the construction or purchase of a good, the financial contribution must be treated as a provision of that good in the sense of Article 1.1(a)(1)(iii). The Panel explained:

"The logic underlying the European Union's argument is that where a particular type of financial contribution is made for the purpose of supporting a firm's financing of the construction or purchase of a good, such a financial contribution must be treated as a provision of that good in the sense of Article 1.1(a)(1)(iii) because of its 'fundamental nature'. Thus, if a government lends money, makes a payment or grants a tax credit to a firm for purposes of reimbursing the firm's acquisition costs, each of these measures would be a financial contribution in the form of a provision of a good or service other than general infrastructure. We consider that this logic is inconsistent with Article 1.1(a)(1), which clearly contemplates a characterization of a measure as a financial contribution on the basis of the manner in which that measure transfers value to a recipient. Therefore, even where they are somehow related to the purchase of goods or services by a recipient, grants, loans, and tax measures are distinctive types of financial contributions. The term 'provide goods or services other than general infrastructure' cannot be interpreted so broadly as to include measures that

¹⁴³ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 965.

¹⁴⁴ Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.388.

¹⁴⁵ Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.388.

¹⁴⁶ (footnote original) Appellate Body Report, *US – Softwood Lumber IV*, para. 69.

¹⁴⁷ Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.389.

fall naturally within the scope of the other types of financial contribution identified in Article 1.1(a)(1)."¹⁴⁸

102. In *US – Softwood Lumber VII*, the Panel agreed with prior panels and the Appellate Body that the purchase of goods under Article 1.1(a)(1)(iii) occurs when a government or public body obtains possession of a good in exchange for a payment of some kind:

"The purchase of goods under Article 1.1(a)(1)(iii) occurs 'when a 'government' or 'public body' obtains possession (including in the form of an entitlement) over a good by making a payment of some kind (monetary or otherwise)'. As we have discussed, above, a benefit will be conferred if the purchase is made for more than adequate remuneration."¹⁴⁹

103. The Panel then examined the alleged financial contribution at issue in the light of this legal standard. The Panel ultimately considered that the alleged financial contribution did not constitute "revenue foregone" in the sense of Article 1.1(a)(1)(ii), and may have been closer to a "purchase of goods" in the sense of Article 1.1(a)(1)(iii). For an examination of the Panel's reasoning, see paragraphs 70 and 71 above.

1.3.5.3 "goods"

104. In *US – Softwood Lumber IV*, the Appellate Body upheld the Panel's finding that nothing in the text of Article 1.1(a)(1)(iii), its context, or the object and purpose of the SCM Agreement supported the conclusion that standing timber is not covered by the term "goods" in Article 1.1(a)(1)(iii). The Panel began by analyzing the ordinary meaning of the term "goods":

"The meaning of a treaty provision, properly construed, is rooted in the ordinary meaning of the terms used. The Panel adopted a definition of the term 'goods', drawn from *Black's Law Dictionary*, put forward in the submissions of both Canada and the United States, that the term 'goods' includes 'tangible or movable personal property other than money'.¹⁵⁰ In particular, the Panel noted that this definition set out in *Black's Law Dictionary* contemplates that the term 'goods' could include 'growing crops, and other identified things to be severed from real property'.¹⁵¹ We observe that the *Shorter Oxford English Dictionary* offers a more general definition of the term 'goods' as including 'property or possessions' especially—but not exclusively—'movable property'.

These definitions offer a useful starting point for discerning the ordinary meaning of the word 'goods'. In particular, we agree with the Panel that the ordinary meaning of the term 'goods', as used in Article 1.1(a)(1)(iii), includes items that are tangible and capable of being possessed. We note, however, as we have done on previous occasions, that dictionary definitions have their limitations in revealing the ordinary meaning of a term. This is especially true where the meanings of terms used in the different authentic texts of the *WTO Agreement* are susceptible to differences in scope. We note that the European Communities, in its third participant's submission, observed that in the French version of the *SCM Agreement*, Article 1.1(a)(1)(iii) addresses, *inter alia*, the provision of '*biens*'. In the Spanish version, the term used is '*bienes*'. The ordinary meanings of these terms include a wide range of property, including immovable property. As such, they correspond more closely to a broad definition of 'goods' that includes 'property or possessions' generally, than with the more limited definition adopted by the Panel. As we have observed previously, in accordance with the customary rule of treaty interpretation reflected in Article 33(3) of the *Vienna Convention on the Law of Treaties* (the '*Vienna Convention*'), the terms of a treaty authenticated in more than one language—like the *WTO Agreement*—are presumed to have the same meaning in each authentic text. It follows that the treaty interpreter should seek the meaning that gives effect, simultaneously, to all the terms of the treaty, as they are used in each authentic language. With this in mind, we find

¹⁴⁸ Panel Report, *US – Large Civil Aircraft (2nd complaint)* (Article 21.5 – EU), para. 8.809.

¹⁴⁹ Panel Report, *US – Softwood Lumber VII*, para. 7.691.

that the ordinary meaning of the term 'goods' in the English version of Article 1.1(a)(1)(iii) of the *SCM Agreement* should not be read so as to exclude tangible items of property, like trees, that are severable from land."¹⁵²

105. After considering the context of the term "goods" in Article 1.1(a)(1)(iii), the Appellate Body considered the consequences of adopting a restrictive interpretation of the scope of Article 1.1(a)(1)(iii):

"[T]o accept Canada's interpretation of the term 'goods' would, in our view, undermine the object and purpose of the *SCM Agreement*, which is to strengthen and improve GATT disciplines relating to the use of both subsidies and countervailing measures, while, recognizing at the same time, the right of Members to impose such measures under certain conditions.¹⁵³ It is in furtherance of this object and purpose that Article 1.1(a)(1)(iii) recognizes that subsidies may be conferred, not only through monetary transfers, but also by the provision of non-monetary inputs. Thus, to interpret the term 'goods' in Article 1.1(a)(1)(iii) narrowly, as Canada would have us do, would permit the circumvention of subsidy disciplines in cases of financial contributions granted in a form other than money, such as through the provision of standing timber for the sole purpose of severing it from land and processing it."¹⁵⁴

106. In *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, the Panel rejected the European Union's argument that patents and other intellectual property rights can be treated as "goods" within meaning of Article 1.1(a)(1)(iii). The Panel recalled that the Appellate Body has only defined "goods" in terms of tangible items in this context and further noted that "the term is typically applied to tangible products, as distinguished from intangible services (a distinction made in the context of trade law and trade policy)."¹⁵⁵ The Panel saw "no basis to extend the sense of goods in this context to encompass all possible forms of property."¹⁵⁶

1.3.5.4 "other than general infrastructure"

107. In *EC and certain member States – Large Civil Aircraft*, the Panel developed an interpretation of the concept of "general infrastructure":

"Dictionaries define the term 'infrastructure' as, *inter alia*, 'installations and services (power stations, sewers, roads, housing, etc.) regarded as the economic foundation of a country,' the 'underlying foundation or basic framework (as of a system or organization),' and the 'system of public works of a country, state, or region.' The term 'general' is defined as 'including, involving, or affecting all or nearly all the parts of a (specified or implied) whole as a territory, community, organization, etc.; completely or nearly universal; not partial, particular, local, or sectional' and 'involving, applicable to, or affecting the whole; involving, relating to, or applicable to every member of a class, kind, or group'. We consider that the term '**general** infrastructure', taken in its ordinary and natural meaning, refers to infrastructure that is not provided to or for the advantage of only a single entity or limited group of entities, but rather is available to all or nearly all entities. In our view, this interpretation is consistent with the ordinary meaning of the term 'general' when used to modify the word 'infrastructure.' However, we consider that it is difficult if not impossible to define the concept of 'general infrastructure' in the abstract.

For us, the existence of limitations on access to or use of infrastructure, whether *de jure* or *de facto*, is highly relevant in determining whether that infrastructure is 'general infrastructure'. However, we are not persuaded by the United States' argument that the existence of *de jure* or *de facto* limitations on access or use is the **only** legally relevant consideration, and one that will always be determinative. We find no support for such a test in the words of Article 1.1(a)(1)(iii), and we see no reason why other considerations concerning the provision of the infrastructure in question

¹⁵² Appellate Body Report, *US – Softwood Lumber IV*, paras. 58-59.

¹⁵⁴ Appellate Body Report, *US – Softwood Lumber IV*, para. 64.

¹⁵⁵ Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.382.

¹⁵⁶ Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.382.

should be categorically excluded from the analysis. In our view, such additional factors could include, *inter alia*, the circumstances under which the infrastructure in question was created and the nature and type of infrastructure in question."¹⁵⁷

108. The Panel emphasized the need for a case-by-case analysis:

"Thus, we do not consider that there is any form or type of infrastructure which is inherently 'general' *per se*. For instance, in our view, such things as railroads or electrical distribution systems do not necessarily constitute 'general infrastructure'.¹⁵⁸ Rather, the determination whether the provision of the good or service in question is 'general infrastructure' or not must be made on a case-by-case basis, taking into account the existence or absence of *de jure* or *de facto* limitations on access or use, and any other factors that tend to demonstrate that the infrastructure was or was not provided to or for the use of only a single entity or a limited group of entities. Such factors may relate to the circumstances surrounding the creation of the infrastructure in question, consideration of the type of infrastructure, the conditions and circumstances of the provision of the infrastructure, the recipients or beneficiaries of the infrastructure, and the legal regime applicable to such infrastructure, including the terms and conditions of access to and/or limitations on use of the infrastructure. If an evaluation of relevant facts concerning such factors demonstrates that the infrastructure was provided to a single entity or a limited group of entities, then we believe it cannot properly be considered 'general' infrastructure, and consequently falls within the scope of Article 1.1(a)(1) of the SCM Agreement, necessitating further analysis to determine whether a subsidy exists."¹⁵⁹

109. In *US – Large Civil Aircraft (2nd complaint)*, the key question of interpretation arising out of the arguments advanced by the parties on the issue of "general infrastructure" was whether the existence of limitations on use or access by the public at large is determinative of whether or not an infrastructure improvement measure is general.¹⁶⁰ The Panel did not consider it necessary to provide a definitive interpretation of the terms "general infrastructure" in Article 1.1(a)(1)(iii) in order to resolve the issues before it.¹⁶¹ However, the Panel noted that it had "some doubts" regarding the argument that even if there are "no limitations on the use of or access to an infrastructure improvement measure by the public", such a measure could nevertheless be found to be something other than "general infrastructure".¹⁶²

1.3.5.5 Purchases of services

110. In *US – Large Civil Aircraft (2nd complaint)*, in a finding that the Appellate Body subsequently declared to be moot and of no legal effect¹⁶³, the Panel found that purchases of services are excluded from the definition of "financial contribution" in Article 1.1(a). Following an analysis of the terms, context, object and purpose, drafting history, and circumstances of the conclusion of the SCM Agreement¹⁶⁴, the Panel concluded that:

"The Panel is not entitled to assume that the disappearance of certain terms from the text of Article 1 of the SCM Agreement 'was merely accidental or an inadvertent oversight on the part of either harassed negotiators or inattentive draftsmen'.¹⁶⁵ The Panel must 'read and interpret the words actually used' in Article 1, not the words that the Panel 'may feel should have been used'.¹⁶⁶ It is not open to the Panel to

¹⁵⁷ Panel Report, *EC and certain member States – Large Civil Aircraft*, paras. 7.1036-7.1037.

¹⁵⁸ (footnote original) Take as an extreme example a 2 kilometer stretch of railway from a mine to a mineral processing plant, used for transporting raw ore for processing, on land owned by the mining company. It seems clear to us that the provision by a government of such a railway cannot properly be considered "general infrastructure" simply because it is a railway.

¹⁵⁹ Panel Report, *EC and certain member States – Large Civil Aircraft*, para. 7.1039.

¹⁶⁰ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.429.

¹⁶¹ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.431.

¹⁶² Panel Report, *US – Large Civil Aircraft (2nd complaint)*, fn 1681.

¹⁶³ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 620.

¹⁶⁴ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 7.953-7.970.

impute into Article 1 'words that are not there'.¹⁶⁷ Having considered the ordinary meaning of the terms of Article 1.1(a)(1)(i), their context, the object and purpose of the SCM Agreement, and the preparatory work and circumstances of the conclusion of the SCM Agreement, the Panel finds that transactions *properly characterized* as purchases of services are excluded from the scope of Article 1.1(a)(1)(i) of the SCM Agreement."¹⁶⁸

111. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body elaborated on the differences between financial contributions set forth in subparagraph (i) and the second sub-clause of subparagraph (iii) of Article 1.1(a)(1):

"With respect to the second sub-clause of subparagraph (iii)—where a government 'purchases goods'—we note that the goods are provided *to* the government by the recipient, in contrast to the first sub-clause of that paragraph, where the goods are provided *by* the government. There are two additional differences between the first and second sub-clauses of subparagraph (iii). The second sub-clause uses the term 'purchase', which is usually understood to mean that the person or entity providing the goods will receive some consideration in return. The other difference is that, in contrast to the first sub-clause that addresses the provision of goods *and services*, the second sub-clause refers only to purchases of 'goods', and not of 'services'."¹⁶⁹

1.3.6 Article 1.1(a)(1)(iv): entrustment or direction of private bodies

112. Article 1.1(a)(1)(iv) was interpreted and applied by the Panels in *US – Export Restraints*¹⁷⁰, *Korea – Commercial Vessels*¹⁷¹, *US – Anti-Dumping and Countervailing Duties (China)*¹⁷², and in three cases on separate countervailing duty investigations of the same Korean support and restructuring programmes and loan guarantees for a Korean DRAM producer: *US – Countervailing Duty Investigation on DRAMS*¹⁷³, *EC – Countervailing Measures on DRAM Chips*¹⁷⁴, and *Japan – DRAMS (Korea)*.¹⁷⁵

113. In *US – Softwood Lumber IV*, the Appellate Body observed that "[p]aragraph (iv) of Article 1.1(a)(1) recognizes that paragraphs (i) – (iii) could be circumvented by a government making payments to a funding mechanism or through entrusting or directing a private body to make a financial contribution".¹⁷⁶

114. The Appellate Body examined Article 1.1(a)(1)(iv) in detail in *US – Countervailing Duty Investigation on DRAMS*. The Appellate Body began by noting that "situations involving exclusively private conduct – that is, conduct that is not in some way attributable to a government or public body – cannot constitute a "financial contribution" for purposes of determining the existence of a subsidy under the *SCM Agreement*".¹⁷⁷ The Appellate Body then explained that Article 1.1(a)(1)(iv) cover situations in which a private body is being used as a "proxy" by the government:

"Paragraphs (i) through (iv) of Article 1.1(a)(1) set forth the situations where there is a financial contribution by a government or public body. The situations listed in paragraphs (i) through (iii) refer to a financial contribution that is provided *directly* by the government through the direct transfer of funds, the foregoing of revenue, the provision of goods or services, or the purchase of goods. By virtue of paragraph (iv), a financial contribution may also be provided *indirectly* by a government where it 'makes payments to a funding mechanism', or, as alleged in this case, where a government 'entrusts or directs a private body to carry out one or more of the type of

¹⁶⁸ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.970.

¹⁶⁹ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 619.

¹⁷⁰ Panel Report, *US – Export Restraints*, paras. 8.15-8.75.

¹⁷¹ Panel Report, *Korea – Commercial Vessels*, paras. 7.350-7.426.

¹⁷² Panel Report, *US – Anti-Dumping and Countervailing Duties (China)*, paras. 12.32-12.38.

¹⁷³ Panel Report, *US – Countervailing Duty Investigation on DRAMS*, paras. 7.10-7.178.

¹⁷⁴ Panel Report, *EC – Countervailing Measures on DRAM Chips*, paras. 7.18-7.146.

¹⁷⁵ Panel Report, *Japan – DRAMS (Korea)*, paras. 7.49-7.254.

¹⁷⁶ Appellate Body Report, *US – Softwood Lumber IV*, para. 52.

¹⁷⁷ Appellate Body Report, *US – Countervailing Duty Investigation on DRAMS*, para.107.

functions illustrated in (i) to (iii) ... which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments'. Thus, paragraphs (i) through (iii) identify the types of actions that, when taken by private bodies that have been so 'entrusted' or 'directed' by the government, fall within the scope of paragraph (iv). In other words, paragraph (iv) covers situations where a private body is being used as a proxy by the government to carry out one of the types of functions listed in paragraphs (i) through (iii). Seen in this light, the terms 'entrusts' and 'directs' in paragraph (iv) identify the instances where seemingly private conduct may be attributable to a government for purposes of determining whether there has been a financial contribution within the meaning of the *SCM Agreement*.¹⁷⁸

115. In *US – Countervailing Duty Investigation on DRAMs*, the Appellate Body also clarified that 'entrustment' occurs where a government gives responsibility to a private body, and 'direction' refers to situations where the government exercises its authority over a private body:

"The term 'entrusts' connotes the action of giving responsibility to someone for a task or an object. ... Delegation is usually achieved by formal means, but delegation also could be informal ... Therefore, an interpretation of the term "entrusts" that is limited to acts of "delegation" is too narrow.

As for the term 'directs' ... in our view, that the private body under paragraph (iv) is directed 'to carry out' a function underscores the notion of authority that is included in some of the definitions of the term 'direct'. ... A 'command' (the word used by the Panel) is certainly one way in which a government can exercise authority over a private body in the sense foreseen by Article 1.1(a)(1)(iv), but governments are likely to have other means at their disposal to exercise authority over a private body. Some of these means may be more subtle than a 'command' or may not involve the same degree of compulsion. Thus, an interpretation of the term 'directs' that is limited to acts of 'command' is also too narrow.

In most cases, one would expect entrustment or direction of a private body to involve some form of threat or inducement, which could, in turn, serve as evidence of entrustment or direction."¹⁷⁹

116. In *US – Countervailing Duty Investigation on DRAMs*, the Appellate Body further observed that Article 1.1(a)(1) (iv) "is intended to ensure that governments do not evade their obligations under the *SCM Agreement* by using private bodies to take actions that would otherwise fall within Article 1.1(a)(1), were they to be taken by the government itself. In other words, Article 1.1(a)(1)(iv) is, in essence, an anti-circumvention provision".¹⁸⁰

117. In *US – Countervailing Duty Investigation on DRAMs*, the Appellate Body agreed with Korea that there must be a demonstrable link between the government and the conduct of the private body. It further stated that "mere policy pronouncements" are insufficient, and that "entrustment and direction" "imply a more active role than mere acts of encouragement" and cannot be "inadvertent or a mere by-product of government regulation":

"It follows, therefore, that not all government acts necessarily amount to entrustment or direction. We note that both the United States and Korea agree that 'mere policy pronouncements' by a government would not, by themselves, constitute entrustment or direction for purposes of Article 1.1(a)(1)(iv). Furthermore, entrustment and direction—through the giving of responsibility to or exercise of authority over a private body—imply a more active role than mere acts of encouragement. Additionally, we agree with the panel in *US – Export Restraints* that entrustment and direction do not cover 'the situation in which the government intervenes in the market in some way, which may or may not have a particular result simply based on the given factual circumstances and the exercise of free choice by the actors in that market'. Thus, government 'entrustment' or 'direction' cannot be inadvertent or a mere by-product of

¹⁷⁸ Appellate Body Report, *US – Countervailing Duty Investigation on DRAMs*, para. 108.

¹⁷⁹ Appellate Body Report, *US – Countervailing Duty Investigation on DRAMs*, paras. 110-111, and 116.

¹⁸⁰ Appellate Body Report, *US – Countervailing Duty Investigation on DRAMs*, para. 113.

governmental regulation. This is consistent with the Appellate Body's statement in *US – Softwood Lumber IV* that 'not all government measures capable of conferring benefits would necessarily fall within Article 1.1(a)'; otherwise paragraphs (i) through (iv) of Article 1.1(a) would not be necessary 'because all government measures conferring benefits, *per se*, would be subsidies.'¹⁸¹

118. The Panel in *US – Supercalendered Paper* considered, based on the Appellate Body's reasoning in *US – Countervailing Duty Investigation on DRAMs*, that a general service obligation to provide electricity was insufficient to determine entrustment or direction:

"The USDOC's determination appears to go counter to the Appellate Body's observation that entrustment and direction do not cover situations "in which the government intervenes in the market in some way, which may or may not have a particular result simply based on the given factual circumstances and the exercise of free choice by the actors in that market". In the facts of the present dispute, it seems that the exercise of free choice is precisely reflected in the fact that Section 52 of the Public Utilities Act does not necessarily result in the provision of electricity to any customer, no matter the terms or conditions. As discussed below, notwithstanding Section 52 of the Public Utilities Act, NSPI only provides electricity to customers if the terms meet certain criteria. If those criteria are not met, no electricity is provided."¹⁸²

119. In *Japan – DRAMs (Korea)*, the Appellate Body recognized that the "commercial unreasonableness" of a financial transaction is a relevant factor in determining the existence of entrustment or direction under Article 1.1(a)(1)(iv):

"We recognize that the commercial unreasonableness of the financial transactions is a relevant factor in determining government entrustment or direction under Article 1.1(a)(1)(iv) of the *SCM Agreement*, particularly where an investigating authority seeks to establish government intervention based on circumstantial evidence. However, this does not mean that a finding of entrustment or direction can never be made unless it is established that the financial transactions were on non-commercial terms. A finding that creditors acted on the basis of commercial reasonableness, while relevant, is not conclusive of the issue of entrustment or direction. A government could entrust or direct a creditor to make a loan, which that creditor then does on commercial terms. In other words, as a conceptual matter, there could be entrustment or direction by the government, even where the financial contribution is made on commercially reasonable terms."¹⁸³

120. In *US – Anti-Dumping and Countervailing Duties (China)*, the Appellate Body reversed the Panel's finding that the term "public body" in Article 1.1(a)(1) of the *SCM Agreement* means "any entity controlled by a government", and found instead that the term "public body" in the context of Article 1.1(a)(1) of the *SCM Agreement* covers only those entities that possess, exercise or are vested with governmental authority. The Appellate Body found support for this interpretation in Article 1.1(a)(1)(iv):

"In seeking to refine our understanding of the concept of 'public body' in Article 1.1(a)(1) of the *SCM Agreement*, and, in particular, of the core characteristics that such an entity must share with government in the narrow sense, we consider next the context provided by Article 1.1(a)(1)(iv). As noted above, this provision introduces the concept of 'private body'. The meaning of the term 'private body' may be helpful in illuminating the essential characteristics of public bodies, because the term 'private body' describes something that is *not* 'a government or any public body'. The panel in *US – Export Restraints* made a similar point when it observed that the term 'private body' is used in Article 1.1(a)(1)(iv) as a counterpoint to government or any public body, that is, any entity that is neither a government in the narrow sense nor a public body would be a private body.

¹⁸¹ Appellate Body Report, *US – Countervailing Duty Investigation on DRAMs*, para. 114.

¹⁸² Panel Report, *US – Supercalendered Paper*, para. 7.62.

¹⁸³ Appellate Body Report, *Japan – DRAMs (Korea)*, para. 138.

The definition of the word 'private' includes 'of a service, business, etc: provided or owned by an individual rather than the state or a public body' and 'of a person: not holding public office or an official position'. We note that both the definition of 'public' and of 'private' encompass notions of authority as well as of control. The definitions differ, most notably, with regard to the subject exercising authority or control.

We also consider that, because the word 'government' in Article 1.1(a)(1)(iv) is used in the sense of the collective term 'government', that provision covers financial contributions provided by a government or any public body where 'a government or any public body' entrusts or directs a private body to carry out one or more of the type of functions or conduct illustrated in subparagraphs (i)-(iii). Accordingly, subparagraph (iv) envisages that a public body may 'entrust' or 'direct' a private body to carry out the type of functions or conduct illustrated in subparagraphs (i)-(iii)."¹⁸⁴

121. In *US – Anti-Dumping and Countervailing Duties (China)*, the Appellate Body also referred to the use of the word "direct" in Article 1.1(a)(1)(iv) in interpreting the term "public body":

"The verb 'direct' is defined as to give authoritative instructions to, to order the performance of something, to command, to control, or to govern an action. The verb 'entrust' means giving a person responsibility for a task. The Appellate Body has interpreted 'direction' as referring to situations where a government exercises its authority, including some degree of compulsion, over a private body, and 'entrustment' as referring to situations in which a government gives responsibility to a private body. Thus, pursuant to subparagraph (iv), a public body may exercise its authority in order to compel or command a private body, or govern a private body's actions (direction), and may be responsible for certain tasks to a private body (entrustment). As we see it, for a public body to be able to exercise its authority over a private body (direction), a public body must itself possess such authority, or ability to compel or command. Similarly, in order to be able to give responsibility to a private body (entrustment), it must itself be vested with such responsibility. If a public body did not itself dispose of the relevant authority or responsibility, it could not effectively control or govern the actions of a private body or delegate such responsibility to a private body. This, in turn, suggests that the requisite attributes to be able to entrust or direct a private body, namely, authority in the case of direction and responsibility in the case of entrustment, are common characteristics of both government in the narrow sense and a public body."¹⁸⁵

122. In *US – Anti-Dumping and Countervailing Duties (China)*, the Appellate Body also considered the phrase "which would normally be vested in the government" in Article 1.1(a)(1)(iv):

"This brings us to the next contextual element, namely, the phrase 'which would normally be vested in the government' in subparagraph (iv). As we see it, the reference to 'normally' in this phrase incorporates the notion of what would ordinarily be considered part of governmental practice in the legal order of the relevant Member. This suggests that whether the functions or conduct are of a kind that are ordinarily classified as governmental in the legal order of the relevant Member may be a relevant consideration for determining whether or not a specific entity is a public body. The next part of that provision, which refers to a practice that, 'in no real sense, differs from practices normally followed by governments', further suggests that the classification and functions of entities within WTO Members generally may also bear on the question of what features are normally exhibited by public bodies."¹⁸⁶

123. In *US – Anti-Dumping and Countervailing Duties (China)*, the Appellate Body also emphasized that:

"[T]he question of whether an entity constitutes a public body is *not* tantamount to the question of whether measures taken by that entity fall within the ambit of

¹⁸⁴ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, paras. 291-293.

¹⁸⁵ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 294.

¹⁸⁶ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 297.

the *SCM Agreement*. A finding that a particular entity does not constitute a public body does not, without more, exclude that entity's conduct from the scope of the *SCM Agreement*. Such measures may still be attributed to a government and thus fall within the ambit of the *SCM Agreement* pursuant to Article 1.1(a)(1)(iv) if the entity is a private entity entrusted or directed by a government or by a public body."¹⁸⁷

124. In *US – Softwood Lumber VII*, the Panel noted that restrictions on exports of a particular product could affect private party behaviour of the suppliers of that product. Noting the USDOC's conclusion, however, that such restrictions had given rise to entrustment or direction by a provincial government to private parties, the Panel considered that entrustment or direction "cannot be a mere by-product of government regulation".¹⁸⁸ The Panel further elaborated as follows:

"Indeed, government regulations of different types could affect private-party behaviour. However, just because a governmental regulation has such an effect does not mean that the *government gives* responsibility to, or the *government exercises* authority over, a private body to provide goods. In particular, we do not consider that a government entrusts or directs a private party to provide goods, or provide them at a particular price, just because that private party's behaviour, in terms of sale and pricing of its goods, is affected by the regulatory framework in which it operates. Therefore, the USDOC's considerations that the LEP process 'discourages log suppliers from considering the opportunities that may exist in the export market', 'restricts the ability of log suppliers to enter into long-term supply contracts with foreign purchasers' and leads to a lower price of timber in British Columbia, pertain in our view to the effects of the export regulation for logs and do not indicate the existence of entrustment and direction."¹⁸⁹

125. Accordingly, the Panel did not consider that a penalty for exporting logs without a permit was a "form of threat or inducement" by a provincial government to ensure that private log suppliers would comply with a law requiring that they supply logs to consumers in British Columbia.¹⁹⁰ The Panel considered that the enactment of measures to enforce a regulation may constitute a threat or inducement to comply with the regulation, and not necessarily a threat or inducement to effectuate a financial contribution in the provision of goods:

"We note that if a government enacts a regulation, it may also enact measures to enforce it, including through penalties. That may be a threat or inducement to comply with the relevant regulation. However, it does not follow that it is a threat or inducement to effectuate a financial contribution in the form of provision of goods, which is what is required under Article 1.1(a)(1)(iv) of the *SCM Agreement*. With regard to the United States' reliance on the USDOC's statement regarding a 'blocking system' that 'creates an environment in which log sellers are forced into informal Agreements that lower export volumes and domestic prices' (which Canada denies), we do not consider that such an arrangement (if any) suggests that it is the government that entrusted or directed the log suppliers to provide goods. In addition, while we note that when mill operators make an offer to purchase advertised logs, the offer is reviewed by the relevant advisory committee to determine whether such offer represents a fair market value (with the authorization to export denied if it is), we also note Canada's explanation that there is no requirement on the log seller to accept those offers. Instead, it could choose to sell to someone else, use the logs themselves or (if in the southern interior of British Columbia) hold off harvesting them in the first place. Therefore, we do not consider that the USDOC had proper basis to conclude that the Governments of British Columbia and Canada gave responsibility to, or exercised their authority over, private log suppliers to provide logs to mill operators."¹⁹¹

¹⁸⁷ Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 302.

¹⁸⁸ Panel Report, *US – Softwood Lumber VII*, para. 7.606.

¹⁸⁹ Panel Report, *US – Softwood Lumber VII*, para. 7.606.

¹⁹⁰ Panel Report, *US – Softwood Lumber VII*, para. 7.607.

¹⁹¹ Panel Report, *US – Softwood Lumber VII*, para. 7.607.

1.3.7 Article 1.1(a)(2): "income or price support"

126. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel, drawing on the interpretation of the term "price support" by the panel in *China – GOES*, interpreted the term "income support" as follows:

"With this understanding of 'price support' as being a direct government intervention to achieve a particular price level for a good, the Panel considers that an 'income support' would be a similar direct government intervention in the market to ensure that income for certain enterprises or associated with certain activities is maintained at or above a particular level. The Panel observes that the French TIRIB does involve an intervention in the market to incentivize the incorporation of the higher-cost biofuels through the application of different levels of tax liability. However, the French TIRIB is not tied to income levels of the taxpayers and it does not ensure that incomes are maintained at or above any particular level."¹⁹²

127. Based on this interpretation, the Panel in *EU and Certain Member States – Palm Oil (Malaysia)* found that the challenged measure, entailing varying levels of a consumption tax depending on the renewable energy contents of fuels, did not constitute income support:

"While the variability factor as an element of the TIRIB formula, considered in isolation, does reduce the amount of tax due under certain conditions, which could then be viewed as supplementing the taxpayers' income net of tax as Malaysia argues, the Panel understands the concept of 'income support' as narrower than a measure that simply reduces tax burden and thereby positively affects after-tax income. An 'income support' would be expected to do more than reduce an expense (thereby permitting more income to be retained) and to do even more than merely add to income through its effects.

Considering the TIRIB as a whole presents a different picture, whereby incomes are neither supplemented nor supported. The French TIRIB creates an additional variable tax on the economic activity of releasing fuel for consumption in France – an activity already taxed by the TICPE and the VAT. In addition, the French TIRIB creates a choice between incorporating qualifying biofuels at greater expense or refraining from such incorporation at the cost of a higher tax burden. From this perspective, the TIRIB overall increases the operating costs for the enterprises that undertake to incorporate the qualifying biofuels and increases the tax burden on the enterprises that do not satisfy the incorporation targets, and neither group of enterprises has their income supported.

For the above reasons, the Panel finds that Malaysia has not established that the French TIRIB measure constitutes or incorporates an 'income support' within the meaning of Article 1.1(a)(2)."¹⁹³

1.3.8 Relationship with other provisions of the SCM Agreement

1.3.8.1 Implications under Article 1.1(b) of the characterization of a transaction under Article 1.1(a)

128. In *Canada – Renewable Energy*, the Appellate Body emphasized that the characterization of a transaction under Article 1.1(a) of the SCM Agreement may have implications for the manner in which the assessment of whether a benefit is conferred is to be conducted under Article 1.1(b).¹⁹⁴

¹⁹² Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, para. 7.1354.

¹⁹³ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1355-7.1357.

¹⁹⁴ Appellate Body Report, *Canada – Renewable Energy*, para. 5.130.

1.3.8.2 Article 14(d)

129. In *US – Countervailing Measures (China)*, the Appellate Body stated that it did not consider that "the fact that the SCM Agreement establishes a single definition for the term 'government' means that, under Article 14(d), a proper analysis for selecting a benefit benchmark is dependent on an examination of whether any relevant entities in the market fall within the definition of 'government', including on the basis of a finding that an SOE is a public body". The Appellate Body observed that the term "government" appears "only" in the first sentence of Article 14(d) and, on this basis, concluded that the "first sentence of Article 14(d) [...] provides guidance for assessing whether the provision of goods confers a benefit, following a previous affirmative determination that such provision of goods constitutes a financial contribution under Article 1.1(a)(1)(iii) that was carried out by a 'government' as defined in Article 1.1(a)(1)."¹⁹⁵

1.3.9 Relationship with other Agreements

1.3.9.1 Agreement on Agriculture

130. In *US – Carbon Steel (India)*, the Appellate Body found that its interpretation of Article 9.1(a) of the Agreement on Agriculture in *Canada – Dairy* is not determinative of its interpretation of the term "public body" in Article 1.1(a)(1) of the SCM Agreement. The Appellate Body came to this conclusion in light of the differences in the text, context, rationale, and object of Article 9.1(a) of the Agreement on Agriculture and Article 1.1 of the SCM Agreement.¹⁹⁶

1.4 Article 1.1(b): "benefit is thereby conferred"

1.4.1 "benefit"

1.4.1.1 General

131. In *US – Large Civil Aircraft (2nd complaint)*, the Appellate Body summarized that a determination of "benefit" under Article 1.1(b) of the SCM Agreement seeks to identify whether the financial contribution has made "the recipient 'better off' than it would otherwise have been, absent that contribution".¹⁹⁷

132. In *India – Sugar and Sugarcane*, in the context of assessing whether financial contributions in the form of grants made to producers of sugar and sugarcane conferred a "benefit" upon sugar mills within the meaning of Article 1.1(b) of the SCM Agreement and therefore constituted subsidies, the Panel noted that:

"Under Article 1.1(b) of the SCM Agreement, a financial contribution by a government is a 'subsidy' if 'a benefit is thereby conferred'. A benefit within the meaning of Article 1.1(b) is an 'advantage' to the recipient of the financial contribution. The term 'benefit', as used in Article 1.1(b), 'implies some kind of comparison' to determine whether 'the 'financial contribution' makes the recipient 'better off' than it would otherwise have been, absent that contribution'. 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."¹⁹⁸

133. The Panel also noted that government grants, by their very nature, confer a benefit:

"[I]n the case of grants, which essentially are gifts from a government, such an inquiry is a simple one. When given to an entity operating in the marketplace, a grant automatically makes the recipient 'better off' than it would otherwise have been

¹⁹⁵ Appellate Body Report, *US – Countervailing Measures (China)*, para. 4.43.

¹⁹⁶ Appellate Body Report, *US – Carbon Steel (India)*, para. 4.26. See also Appellate Body Report, *US – Anti-Dumping and Countervailing Duties (China)*, para. 330.

¹⁹⁷ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, paras. 635–636, 662, and 690.

¹⁹⁸ Panel Report, *India – Sugar and Sugarcane*, para. 7.257.

because it gives that recipient greater resources than it had before, to allow it to pursue its commercial aims, and the grant does not entail any specific reciprocal obligation on the part of the recipient."¹⁹⁹

134. On the basis of this reasoning, the Panel concluded that the financial contributions in question were subsidies because they conferred a benefit upon sugar mills within the meaning of Article 1.1(b) of the SCM Agreement:

"Under the Production Assistance, Buffer Stock, and Marketing and Transportation Schemes, sugar mills receive assistance from the Central Government, which is aimed at enabling them to clear their sugarcane dues to farmers. Although, pursuant to the payment arrangements under the three Schemes, the assistance is credited by the Central Government directly into the accounts of sugarcane farmers on behalf of sugar mills, we consider that the benefit accrues to sugar mills and not to farmers. Such assistance is gratuitous, and thus constitutes grants. In our view, by receiving such grants, sugar mills are automatically placed in a better position than they would have been absent the grants, and thus receive a benefit."²⁰⁰

135. In *Canada – Renewable Energy*, the Appellate Body noted the implications of the characterization of a transaction under Article 1.1(a) of the SCM Agreement for the determination of whether a benefit has been conferred:

"[T]he characterization of a transaction under Article 1.1(a) of the SCM Agreement may have implications for the manner in which the assessment of whether a benefit is conferred is to be conducted. For instance, the context provided by Article 14 of the SCM Agreement presents different methods for calculating the amount of a subsidy in terms of benefit to the recipient depending on the type of financial contribution at issue. However, although different characterizations of a measure may lead to different *methods* for determining whether a benefit has been conferred, the issue to be resolved under Article 1.1(b) remains to ascertain whether a 'financial contribution' or 'any form of income or price support' has conferred a benefit to the recipient."²⁰¹

1.4.1.2 Advantage *vis-a-vis* the market

136. The Panel in *Canada – Aircraft* found that "the only logical basis" for determining whether the financial contribution places the recipient in a more advantageous position than it otherwise would have been "is the market".²⁰² According to the Panel:

"[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."²⁰³

137. In *Canada – Renewable Energy*, the Appellate Body stated that a panel tasked with a benefit determination should begin its analysis by defining the relevant market. It further stated that the "definition of the relevant market is central to, and a prerequisite for, a benefit analysis under Article 1.1(b) the SCM Agreement".²⁰⁴

138. The Appellate Body upheld the Panel's finding that "benefit" must be established by determining whether the financial contribution makes the recipient better off *vis-à-vis* the market than it would have been absent that financial contribution:

"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

¹⁹⁹ Panel Report, *India – Sugar and Sugarcane*, para. 7.259.

²⁰⁰ Panel Report, *India – Sugar and Sugarcane*, para. 7.261.

²⁰¹ Appellate Body Report, *Canada – Renewable Energy*, para. 5.130.

²⁰² Panel Report, *Canada – Aircraft*, para. 9.112.

²⁰³ Panel Report, *Canada – Aircraft*, para. 9.112.

²⁰⁴ Appellate Body Report, *Canada – Renewable Energy*, para. 5.169.

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.

Article 14, which we have said is relevant context in interpreting Article 1.1(b), supports our view that the marketplace is an appropriate basis for comparison."²⁰⁵

139. In *US – Supercalendered Paper*, the Panel considered the crucial question in establishing benefit to be whether or not the company in question would have been better off absent the government funding. In this case, the funding provided did not result in company "receiving anything more than it paid for".²⁰⁶

140. The Panel in *US – Supercalendered Paper* emphasized the importance of market principles in determining the existence of a benefit, and noted that the USDOC had failed to take into consideration evidence showing that the programme at issue "had indeed resulted from negotiations based on market considerations."²⁰⁷

141. Along the same lines, the Appellate Body in *EC and certain member States – Large Civil Aircraft* approached the assessment of benefit as "one that is financial in nature and in which the behaviour of the grantor and recipient of the alleged subsidy at issue are assessed against the behaviour of commercial actors in the market"; and one that requires an examination of "the terms and conditions that would have been offered in the market at that time".²⁰⁸

142. The Appellate Body in *EC and certain member States – Large Civil Aircraft* further stated that "[t]he comparison is to be performed as though the [actual and benchmark] loans were obtained at the same time" and noted that "the assessment focuses on the moment in time when the lender and borrower commit to the transaction".²⁰⁹

143. Based on the above guidance from the Appellate Body in *EC and certain member States – Large Civil Aircraft*, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* rejected an "averaging approach" to calculate benefit over a time-period.²¹⁰ The Panel noted that "[a]veraging the borrowing rate of contracts concluded over a time-period during which there were different market borrowing rates may lead to distortions" and could lead to a "misplaced" finding of subsidization.²¹¹ In addition, the Panel considered such an "averaging approach" inconsistent with Appellate Body guidance that "(a) the benchmark entails a consideration of what a market participant would have been able to secure on the market at that time, and (b) that the assessment focuses on the moment in time when the lender and borrower commit to the transaction."²¹² The Panel therefore concluded the appropriate approach to be a calculation "of the yields from a consistent time-period up to the date of the conclusion of the individual contract".²¹³

144. The Appellate Body in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* noted that when identifying the appropriate market benchmark rate of return for assessing whether the financial contribution conferred a benefit on the recipient, market data on the bond yield that is closer in time to the conclusion of the terms and conditions between the lender and borrower of a loan will usually be more probative than data derived from time periods preceding the final stages of negotiating and concluding the loan. Nevertheless, a panel's assessment of the appropriate timing of the conclusion of terms and conditions must be made on a case-by-case basis taking into account several factors. The Appellate Body noted that in certain circumstances, particularly in the case of complex financial instruments where the terms and conditions of the loan have been negotiated and agreed over a certain contracting period, it would be appropriate

²⁰⁵ Appellate Body Report, *Canada – Aircraft*, paras. 157 and 158. See also Appellate Body Report, *Canada – Renewable Energy*, para. 5.163.

²⁰⁶ Panel Report, *US – Supercalendered Paper*, para. 7.106.

²⁰⁷ Panel Report, *US – Supercalendered Paper*, para. 7.77.

²⁰⁸ Appellate Body Report, *US – Large Civil Aircraft (2nd complaint)*, para. 636 (referring to Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, paras. 706 and 836).

²⁰⁹ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, paras. 835-836.

²¹⁰ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.388.

²¹¹ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.385.

²¹² Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.388.

²¹³ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.388.

for a panel to take into account in its analysis information that pre-dates the moment or actual day on which the legal instruments underlying the relevant transaction were formally signed:

"A meaningful benefit analysis pursuant to Article 1.1(b) requires panels to carry out a careful and thorough comparison between the financial contribution provided by a government and a market benchmark. Regarding the manner in which the timing of the relevant transactions should be factored into the benefit analysis, we reiterate that the benefit comparison must be undertaken on an *ex ante* basis, and thus focuses on the moment in time when the lender and borrower commit to the transaction. Information that is closer in time to the conclusion of the terms and conditions of a loan will usually be more probative than information that derives from time periods preceding the final stages of negotiations and conclusion of a transaction. Nevertheless, a panel's determination regarding the appropriate timing of when the lender and borrower committed to the relevant terms and conditions of the transaction at issue should be made on a case-by-case basis, taking into account the specific nature and features of the financing at issue and in light of the arguments and evidence presented by the parties.

A panel conducting this assessment must look at how the relevant government financial contribution is structured, focusing on the nature and type of financing that is being provided and whether aspects thereof were agreed upon in the period leading up to the formal signing of the legal instrument providing the financial contribution may commit to a complex financing instrument only after all the relevant terms and conditions in their overall configuration are known, it is also possible to envisage cases where parties may have committed to a transaction – or to key aspects thereof – during a finalization period of the negotiations preceding the moment of formal conclusion of *all* aspects of that transaction. This may be the case, in particular, where the financial contribution at issue consists of complex financing instruments, the terms and conditions of which have been negotiated and agreed over a certain contracting period. In such circumstances, it would be appropriate for a panel to take into account in its analysis information that pre-dates the moment or actual day on which the legal instruments underlying the relevant transaction were formally signed, bearing in mind that information closer in time to the formal conclusion of the financing instrument will be more probative than information from earlier stages of the negotiations."²¹⁴

145. The Appellate Body in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* disagreed with the European Union to the extent that it suggested that the Panel was required to limit its analysis to data from the day of conclusion of each A350XWB LA/MSF contract regardless of the time period over which the parties may have committed to the terms and conditions of that financing instrument.²¹⁵

146. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* also considered whether it would be appropriate to incorporate an adjustment to represent normal fees and charges for the calculation of a market benchmark to determine whether the LA/MSF measures at issue confer a "benefit". The Panel stated:

"In our view, it is not necessary that any fees charged for the lending at issue be 'analogous' to the commercial fees charged by a market lender in order for it to be appropriate to include such fees into the relevant market benchmark. Indeed, such an approach would neglect the potentially advantageous waiver of any such fees that might be relevant to a benefit analysis.

We therefore consider that, in principle, a difference between the sums that the market would have generally charged by way of normal fees and expenses for comparable financing to LA/MSF, and the amounts, if any, charged by the relevant

²¹⁴ Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 5.119–5.120.

²¹⁵ Appellate Body Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 5.184.

member State for LA/MSF financing, should be factored into a consideration of whether a benefit has been conferred."²¹⁶

147. According to this "benchmark" analysis, the Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* found that the A350XWB LA/MSF measures at issue conferred a "benefit" to the firm Airbus under Article 1.1(b) of the SCM Agreement.²¹⁷ The Panel also found support for its finding in certain evidence on the record. First, government evaluations and statements suggested the A350XWB LA/MSF project contract was not provided on commercial terms (e.g. official statements by the United Kingdom described participation in the project as "essential" and referred to "a clearly identified need" for funding).²¹⁸ Second, the Panel noted that a commercial investor would normally perform due diligence before entering into a loan contract; however, the absence of such written project appraisals, analyses, or evaluations of the A350XWB project suggested the existence of "benefit" and subsidization:

"[A] commercial investor would be normally expected to perform a certain degree of due diligence in relation to the current and future 'economic conditions' of a particular project before agreeing to enter into a loan contract. In our view, the conclusions we have reached about the method and facts used by the European Union member States to inform their decisions to agree to provide Airbus ... in A350XWB LA/MSF suggest that they have each, to differing degrees, fallen short of the standard that one would expect a commercial lender to normally satisfy. As we see it, this evidence suggests that the European Union member States entered into the A350XWB LA/MSF contracts in a manner that is inconsistent with that of a commercial lender, thereby confirming our finding of subsidisation."²¹⁹

148. Numerous dispute settlement reports confirm that a financial contribution confers a "benefit" if it is provided to the recipient on terms more favourable than the recipient could have obtained from the market.²²⁰ The Panel in *US – Large Civil Aircraft (2nd complaint)* observed that it is now "well established" that a financial contribution confers a benefit within the meaning of Article 1.1(b) of the SCM Agreement if the terms of the financial contribution are more favourable than the terms available to the recipient in the market.²²¹

149. Following a similar logic, the compliance Panel in *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)* considered that the Space Act Agreements, between the NASA and Boeing, at issue conferred a "benefit" within the meaning of Article 1.1(b) because "the allocation of patent rights and related licence rights is more favourable to Boeing than the allocation of patent rights and related licence rights under the private collaborative R&D agreements before the Panel, and that Boeing may additionally request that NASA restrict access to data that allows use for commercial purposes".²²²

150. In determining the relevant market for a benefit analysis, the Appellate Body has found that both demand-side and supply-side considerations should be taken into account.²²³

151. The Panel in *India – Export Related Measures* found that the duty and tax exemptions and deductions at issue, granted by India under various Schemes, conferred a benefit upon their

²¹⁶ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.426-6.247.

²¹⁷ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.634.

²¹⁸ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, paras. 6.652-6.654.

²¹⁹ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.651.

²²⁰ See e.g. Panel Reports, *Canada – Aircraft*, para. 9.112; and *Brazil – Aircraft*, para. 7.24; Appellate Body Report, *Canada – Aircraft*, paras. 154 and 157; Panel Reports, *Korea – Commercial Vessels*, para. 7.427; and *EC – Countervailing Measures on DRAM Chips*, para. 7.176; Appellate Body Reports, *Japan – DRAMs (Korea)*, para. 225; *EC and certain member States – Large Civil Aircraft*, para. 705; and *US – Large Civil Aircraft (2nd complaint)*, paras. 635 – 636.

²²¹ Panel Report, *US – Large Civil Aircraft (2nd complaint)*, para. 7.475.

²²² Panel Report, *US – Large Civil Aircraft (2nd complaint) (Article 21.5 – EU)*, para. 8.195.

²²³ Appellate Body Reports, *Canada – Renewable Energy*, para. 5.171; *EC and certain member States – Large Civil Aircraft*, para. 1121.

recipients, by making them better off than they would be in the market, absent those exemptions and deductions.²²⁴ According to the Panel:

"As others before us, we note that 'relief from taxation otherwise due is not generally available to market participants, nor does it exist as a general condition in the marketplace'. Beginning with the exemptions from customs duties on importation, we observe that an importer of goods under the EOU/EHTP/BTP Schemes, EPCG Scheme, SEZ Scheme, or DFIS, gets to import goods free of customs duties. The market – however defined – does not offer this 'gift'. An importer of the very same goods outside these or other exemption schemes is subject to customs duties. Thus, a recipient of the customs duty exemption under the EOU/EHTP/BTP Schemes, EPCG Scheme, SEZ Scheme, or DFIS is 'better off' than it would otherwise have been, absent that contribution.

...

Similar considerations are also valid for the deduction from taxable income under the SEZ Scheme. To recall, SEZ entrepreneurs are allowed to deduct profits and gains from exports from the total income of their Units, to which income tax is applied. By contrast, entities outside the SEZ Scheme have to pay tax on such income. Again, this makes SEZ entrepreneurs and their Units better off than they would be in the absence of the financial contribution – i.e. better off than if they had to pay tax on their export income."²²⁵

152. In *US – Softwood Lumber VII*, the Panel agreed with the understanding of Article 1.1(b) set out in prior panel and Appellate Body reports that a financial contribution will only confer a benefit if it is provided on terms that are more advantageous than those that would have been available to the recipient in the market.²²⁶

153. In the light of this understanding, the Panel then examined the USDOC's determination of whether the purchase of biomass electricity by a state-owned company (BC Hydro) from two companies conferred a benefit. The Panel noted that the USDOC compared BC Hydro's purchase price of biomass electricity from the two companies to BC Hydro's tariff rates applied to electricity generated from all sources purchased from the two companies. The Panel considered the USDOC's approach to be "fundamentally flawed"²²⁷, as the USDOC selected a benchmark reflecting the prevailing market conditions for the sale of electricity at the retail level, whereas the prevailing market conditions were shaped by a different regulatory regime that required it, at the wholesale level, to purchase electricity generated from biomass.²²⁸ Specifically, the Panel stated the following:

"In considering the benchmark the USDOC selected, we note that the relevant financial contribution is the purchase by BC Hydro of electricity generated by Tolko and West Fraser from biomass. In purchasing electricity, BC Hydro was bound by the requirements of the BC Energy Plan, which required it to purchase electricity generated from biomass. In the context of *that* regulatory regime, electricity generated by Tolko and West Fraser was not substitutable – from BC Hydro's perspective – with electricity generated from other sources. As a result, the fact that BC Hydro did not track the source of electricity that it sells to *its* customers, or the fact that there was no information on the record to demonstrate that the method used to generate electricity changes the physical characteristics or the fungibility of electricity, is not determinative. The regulatory regime imposed by the BC Energy Plan shaped the prevailing market conditions governing the sale and purchase of electricity at the wholesale level. The fact that a regulatory regime shapes the wholesale electricity market in British Columbia is not, in and of itself, a cause of subsidization.

²²⁴ Panel Report, *India – Export Related Measures*, para. 7.458.

²²⁵ Panel Report, *India – Export Related Measures*, paras. 7.451 and 7.453.

²²⁶ Panel Report, *US – Softwood Lumber VII*, paras. 7.637-7.638.

²²⁷ Panel Report, *US – Softwood Lumber VII*, para. 7.648.

²²⁸ Panel Report, *US – Softwood Lumber VII*, paras. 7.648-7.650.

Accordingly, the benchmark selected by the USDOC should have reflected these prevailing market conditions for electricity at the wholesale level. By selecting a benchmark that reflected prevailing market conditions for the sale of electricity at the *retail* level, where the prevailing market conditions were not shaped by the same regulatory regime, the USDOC acted inconsistently with Articles 1.1(b) and 14(d) of the SCM Agreement."²²⁹

154. The Panel also examined the USDOC's benefit analysis concerning payments made by BC Hydro to a company, Tolko, in the context of an electricity purchase agreement (EPA) between BC Hydro and Tolko. Pursuant to this EPA, BC Hydro required Tolko to set aside an agreed amount of electricity for BC Hydro, prohibited Tolko from selling this specified amount electricity to any third parties, and agreed that it would make payments to Tolko should it decline ultimately to purchase the set-aside electricity from Tolko (turn-down payments).²³⁰ The Panel considered that the USDOC failed to identify an appropriate benchmark for the turn-down payments, as the USDOC had treated the payments as a "grant", as opposed to a conveyance of funds involving a reciprocal obligation on the part of the recipient:

"It is undisputed that in the case of a grant 'the conveyance of funds will not involve a reciprocal obligation on the part of the recipient'. The issue before us, therefore, is whether the USDOC erred in finding that the turn-down payments BC Hydro made to Tolko did *not* involve a reciprocal obligation and as a result, if the USDOC failed to assess whether a benefit was conferred consistent with Article 1.1(b). We consider that the record evidence clearly indicates that the turn-down payments were part of the contractual obligation between BC Hydro and Tolko for the purchase of electricity, with reciprocal obligations clearly imposed on Tolko. We disagree with the arguments of the United States that BC Hydro did not receive anything in return for its payments, since these payments were made according to the provision of the EPA that guarantees the supply of electricity exclusively to BC Hydro and compensates Tolko's costs to generate electricity if BC Hydro turns down the electricity."²³¹

155. The Panel ultimately found that the USDOC failed to assess whether a benefit was conferred consistent with Article 1.1(b). The Panel also found that the USDOC acted inconsistently with the first sentence of Article 14(d) in that, after improperly treating the turn-down payments as grants, it failed to assess whether the purchase of goods was made for more than adequate remuneration.²³²

156. In *EU and Certain Member States – Palm Oil (Malaysia)*, the Panel made the following observations about the existence of benefit in cases where financial contribution takes the form of government revenue foregone:

"The Panel considers that where a government purchases goods or services, sells goods, loans money, infuses equity and so on, there can be an important distinction between the question of a financial contribution being made and a benefit being conferred because the government could take the above actions at market prices or market rates. In such cases, the recipient of the financial contribution would be no better off than if they engaged in the same transaction with a private commercial entity on commercial terms. In the case of government revenue otherwise due that is foregone or not collected, it has been considered that such financial contributions are not available in the market. A recipient of a financial contribution in the form of government revenue foregone or not collected receives a benefit equal to the amount of tax otherwise due that was foregone or not collected. This has been considered to be so even where the taxpayer is induced to undertake some actions and incur associated expenses to qualify for the tax break. In this case the taxpayers do incur additional production costs to incorporate qualifying biofuels into the fuel mix and they are induced to do so to take advantage of the tax reduction. Because they choose to incorporate the costlier biofuels into their fuel mix to take advantage of the tax

²²⁹ Panel Report, *US – Softwood Lumber VII*, paras. 7.649-7.650.

²³⁰ Panel Report, *US – Softwood Lumber VII*, para. 7.659.

²³¹ Panel Report, *US – Softwood Lumber VII*, para. 7.662.

²³² Panel Report, *US – Softwood Lumber VII*, para. 7.664.

reductions, it can be reasoned that a benefit has been conferred on them by doing so."²³³

157. However, the Panel in *EU and Certain Member States – Palm Oil (Malaysia)* also cautioned against assuming that the benefit thus conferred upon the tax payers (sellers of fuel) automatically extends to the downstream producers of biofuels that make the fuel qualify for the revenue foregone:

"The Panel considers that the above rationale cannot be applied to assume that a benefit conferred in the form of a lower tax liability on the taxpayers, who are operators releasing fuel for consumption in France under the French TIRIB, will necessarily automatically confer a benefit upon the upstream suppliers of qualifying biofuels or on the producers of qualifying biofuels. The Panel considers that Malaysia has not provided sufficient additional information and argument to establish that under the circumstances of this case the conferral of a benefit should be considered to extend beyond the group of taxpayers.

For the above reasons, the Panel considers that, on the *arguendo* assumption that a financial contribution exists as described above, a benefit would thereby be conferred on the operators that release fuel for consumption in France incorporating some portion of qualifying biofuels. The Panel considers that Malaysia has not established that the conferral of a benefit should be considered to extend beyond this group of taxpayers."²³⁴

1.4.1.3 Benefit to recipient vs. cost to government

158. In *Canada – Aircraft*, Canada argued that a financial contribution only conferred a "benefit" to the extent that it resulted in a net cost to the government. The Panel rejected Canada's argument, finding that the ordinary meaning of "benefit" does not include any notion of net "cost to the government".²³⁵ According to the Panel, the ordinary meaning of "benefit" instead "clearly encompasses some form of advantage."²³⁶ To establish the existence of that advantage, the Panel found that "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."²³⁷ The Panel's finding that benefit is determined by reference to the situation of the recipient, rather than any cost to the government, was upheld by the Appellate Body:

"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. This provides textual support for the view that the focus of the inquiry under Article 1.1(b) of the *SCM Agreement* should be on the recipient and not on the granting authority. The ordinary meaning of the word 'confer', as used in Article 1.1(b), bears this out. 'Confer' means, *inter alia*, 'give', 'grant' or 'bestow'. The use of the past participle 'conferred' in the passive form, in conjunction with the word 'thereby', naturally calls for an inquiry into *what was conferred on the recipient*. Accordingly, we believe that Canada's argument that 'cost to government' is one way of conceiving of 'benefit' is at odds with the ordinary meaning of Article 1.1(b), which focuses on the *recipient* and not on the *government* providing the 'financial contribution'."²³⁸

1.4.1.4 The relevant recipient – scope of the SCM Agreement

159. In *Brazil – Aircraft (Article 21.5 – Canada II)*, the underlying subsidy took the form of government payments to lenders in support of export credit transactions, i.e. financial services. The Panel found that without such support, export credit would likely not have been made

²³³ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, para. 7.1366.

²³⁴ Panel Report, *EU and Certain Member States – Palm Oil (Malaysia)*, paras. 7.1367-7.1368.

²³⁵ Panel Report, *Canada – Aircraft*, para. 9.112.

²³⁶ Panel Report, *Canada – Aircraft*, para. 9.112.

²³⁷ Panel Report, *Canada – Aircraft*, para. 9.112.

²³⁸ Appellate Body Report, *Canada – Aircraft*, para. 154.

available to purchasers of regional aircraft. The Panel provided the following clarification regarding the scope of the SCM Agreement:

"In considering whether PROEX III payments confer a benefit, the Panel notes that the financial contribution in this case is in the form of a (non-refundable) payment, rather than in the form of a loan. As a usual matter, of course, a non-refundable payment will confer a benefit. Thus, there would be no need for complex benefit analysis if PROEX III payments were made directly to producers or to purchasers of Brazilian regional aircraft. In this case, however, the payment is not provided to a producer of regional aircraft. Rather, PROEX III payments are provided *to a lender* in support of an export credit transaction relating to Brazilian regional aircraft. Thus, while there can be no doubt that PROEX III payments confer a benefit, we consider that the question remains whether PROEX III payments confer a benefit to *producers of regional aircraft*. ... [W]hether the financial contribution has conferred a benefit to producers of regional aircraft -- as opposed merely to a benefit to suppliers of financial services -- depends upon the impact of PROEX III payments on the terms and conditions of the export credit financing available to purchasers of Brazilian regional aircraft."²³⁹

160. The Panel further clarified its reasoning in two footnotes:

"As the *SCM Agreement* is an Annex 1A agreement on trade in *goods*, and as this case relates to alleged export subsidies in respect of a particular good -- Brazilian regional aircraft -- it is incumbent upon Canada to establish that the benefit derived from PROEX III payments is not retained exclusively by the lender but rather is passed through in some way to producers of regional aircraft."²⁴⁰

161. In terms of the burden of proof on the complaining party in such cases, the Panel explained that proof of subsidized financial services to the customer would constitute *prima facie* proof of benefit to the producer:

"We note that PROEX III payments are made in support of export credits extended to the *purchaser*, and not to the *producer*, of Brazilian regional aircraft. In our view, however, to the extent Canada can establish that PROEX III payments allow the purchasers of a product to obtain export credits on terms more favourable than those available to them in the market, this will, at a minimum, represent a *prima facie* case that the payments confer a benefit on the *producers* of that product as well, as it lowers the cost of the product to their purchasers and thus makes their product more attractive relative to competing products."²⁴¹

162. The Panel in *Canada – Aircraft Credits and Guarantees* endorsed the approach taken in *Brazil – Aircraft (Article 21.5 – Canada II)*.²⁴²

1.4.1.5 Evidence establishing the existence of benefit

163. The Panel in *Japan – DRAMs (Korea)* acknowledged the evidentiary problems that may arise in seeking to establish "benefit" by reference to the market, particularly where no "market" benchmark exists:

"As noted above, it is now well established that the concept of benefit is defined by reference to the market, such that a financial contribution confers a 'benefit' within the meaning of Article 1.1(b) of the *SCM Agreement* when it is made available on terms that are more favourable than the recipient could have obtained on the market. While an investigating authority must apply this standard on the basis of relevant evidence, there are no provisions in the *SCM Agreement* regarding the precise nature of the evidence on which an investigating authority must rely. The guidelines set forth in Article 14 of the *SCM Agreement* offer some guidance on the types of evidence that

²³⁹ Panel Report, *Brazil – Aircraft (Article 21.5 – Canada II)*, paras. 5.27.

²⁴⁰ Panel Report, *Brazil – Aircraft (Article 21.5 – Canada II)*, fn 41.

²⁴¹ Panel Report, *Brazil – Aircraft (Article 21.5 – Canada II)*, fn 42.

²⁴² Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.229.

might be relevant. However, the Article 14 guidelines do not cover all eventualities. For example, Article 14(b) does not indicate how an investigating authority should establish the existence of benefit conferred by a loan in the event that there are no 'comparable commercial loans which the firm could actually obtain on the market'.

In certain circumstances, an investigating authority might examine the existence of benefit by gathering available evidence of the terms that the market would have offered, and by comparing those terms with those of the financial contribution at issue. This is the approach advocated by Korea in the present case. In other circumstances, an investigating authority might rely on evidence of whether or not the financial contribution was provided on the basis of commercial considerations. This is the approach adopted by the JIA in the present case. In our view, both types of evidence are relevant in determining the existence of benefit. The first, because such evidence provides a market benchmark against which to determine whether or not the terms on offer were more favourable than those available from the market. The second, because evidence of reliance on non-commercial considerations indicates terms more favourable than those available from the market (as the market is presumed to operate on the basis of commercial considerations).²⁴³ Depending on the particular circumstances of a case, an investigating authority might also rely on other types of evidence that could be equally relevant."²⁴⁴

164. The Panel in *Japan – DRAMs (Korea)* went on to note that:

"An investigating authority might also be confronted with both types of evidence described above, and one type of evidence might not support the conclusion suggested by the other. For example, there might be evidence that, although the financial contribution was not provided on the basis of commercial considerations, it would in fact have been provided by 'creditors acting in accordance with the 'usual practice' in the relevant market'. In such cases, the investigating authority would need to weigh the probative value of one type of evidence against the probative value of the other."²⁴⁵

165. On appeal from this finding, Korea argued that an entity's failure to undertake an analysis based on commercial considerations does not necessarily mean that a benefit is conferred. According to Korea, an entity might arrive at a market result without applying market considerations. Without specifically addressing Korea's argument, the Appellate Body upheld the Panel's reliance on evidence regarding reliance on non-commercial considerations.²⁴⁶

166. In *Canada – Renewable Energy*, the Appellate Body considered government-administered prices. The Appellate Body stated that government-administered prices may or may not reflect what a hypothetical market would yield and that "the fact that the government sets prices does not in itself establish the existence of a benefit".²⁴⁷ Furthermore, the Appellate Body provided guidance on how to conduct an analysis in such cases:

"In challenging a benefit comparison under Article 1.1(b) of the SCM Agreement, a complainant would have to show that such prices do not reflect what a market outcome would be. An analysis of the methodology that was used to establish the administered prices may provide evidence as to whether the price does or does not provide more than adequate remuneration. There may be circumstances where there is no information about the methodology that was used or the methodology used does not assist in determining whether the administered price is or is not reflective of what a market would yield. If it becomes necessary to identify a market benchmark or to construct a proxy, such benchmark or proxy may be administered prices for the same

²⁴³ (footnote original) We note that such an approach to determining the existence of benefit was upheld by the panel in *EC – Countervailing Measures on DRAM Chips*. That panel upheld the investigating authority's finding of benefit in respect of the October 2001 restructuring on the basis that the investigating authority had reasonably concluded that none of the non-entrusted / directed creditors had acted "in a commercially reasonable manner". (*EC – Countervailing Measures on DRAM Chips*, para. 7.209)

²⁴⁴ Panel Report, *Japan – DRAMs (Korea)*, paras. 7.275-7.276.

²⁴⁵ Panel Report, *Japan – DRAMs (Korea)*, fn 475.

²⁴⁶ Appellate Body Report, *Japan – DRAMs (Korea)*, para. 226.

²⁴⁷ Appellate Body Report, *Canada – Renewable Energy*, para. 5.228.

product (in the country of purchase or in other countries, subject to adjustments), provided that it is determined based on a price-setting mechanism that ensures a market outcome. Alternatively, such benchmark may also be found in price-discovery mechanisms such as competitive bidding or negotiated prices, which ensure that the price paid by the government is the lowest possible price offered by a willing supply contractor."²⁴⁸

167. In *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, the Panel stated, where possible, "it is preferable to derive a market benchmark on the basis of data pertaining to the borrowing entities' own market-based borrowing, rather than generic estimates" to establish "benefit".²⁴⁹ The Panel explained:

"We recall that it is well established that a 'financial contribution' will confer a 'benefit' upon a recipient when it places that recipient in a more advantageous position compared with the position of that recipient in the absence of the financial contribution. We consider that a market benchmark should approximate as closely as possible lending on the same, or similar, terms and conditions to the particular recipient. We find support for this understanding in the context provided by Article 14(b) of the SCM Agreement, which provides that:

'A loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that *the firm* receiving the loan pays on the government loan, and the amount *the firm* would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts. (emphasis added)'"²⁵⁰

168. The Panel in *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)* addressed evidence relevant to the benefit analysis. The United States had relied on government statements and media reports to demonstrate that the challenged measures were not commercially available and thereby conferred a "benefit" to Airbus within meaning of Article 1.1(b) of the SCM Agreement. The European Union argued such evidence was not sufficient to demonstrate the measures conferred a "benefit". The Panel disagreed with the European Union:

"To the extent that the European Union's submissions imply that the only evidence relevant to the benefit analysis that we must perform in this dispute is a comparison of rates, we disagree. While the analysis of whether a financial contribution involving a direct transfer of funds confers a 'benefit' would usually involve comparing rates of return with a market benchmark rate, we do not preclude that other evidence may be relevant as to whether or not a benefit is conferred."²⁵¹

1.4.1.6 Government interventions that create markets vs. government interventions in support of certain players in the market

169. In *Canada – Renewable Energy*, the Appellate Body indicated that a distinction should be drawn between government interventions that create markets that would otherwise not exist and, other types of government interventions in support of certain players in markets that already exist, or to correct market distortions therein. The Appellate Body distinguished the two by noting:

"Where a government creates a market, it cannot be said that the government intervention distorts the market, as there would not be a market if the government had not created it. While the creation of markets by a government does not *in and of itself* give rise to subsidies within the meaning of the SCM Agreement, government interventions in existing markets may amount to subsidies when they take the form of

²⁴⁸ Appellate Body Report, *Canada – Renewable Energy*, para. 5.228.

²⁴⁹ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.361.

²⁵⁰ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.362.

²⁵¹ Panel Report, *EC and certain member States – Large Civil Aircraft (Article 21.5 – US)*, para. 6.302.

a financial contribution, or income or price support, and confer a benefit to specific enterprises or industries."²⁵²

1.4.2 "is ... conferred"

1.4.2.1 General

170. In *US – Lead and Bismuth II*, the United States argued that the present tense of the verb "is conferred" in Article 1.1 of the SCM Agreement shows that an investigating authority must demonstrate the existence of "benefit" only at the time the "financial contribution" was made. The consequence of this argument was that an investigating authority would not be required to make a finding of benefit in a (subsequent) review of the countervailing measure. The United States asserted that "if WTO Members were required to conduct an 'ongoing demonstration' that the original benefit still constitutes an advantage to the relevant company, it would become 'nearly impossible' to administer countervailing duty laws."²⁵³ The Appellate Body in *US – Lead and Bismuth II* rejected the United States' argument, holding that "Article 1.1 does not address the *time* at which the 'financial contribution' and/or the 'benefit' must be shown to exist."²⁵⁴ On this basis, the Appellate Body found that an investigating authority may, in certain circumstances, be required to confirm the continued existence of benefit, even after countervailing duties have been imposed.²⁵⁵

1.4.2.2 Mandatory/discretionary conferral of a benefit

1.4.2.2.1 Challenging subsidy programmes "as such"

1.4.2.2.1.1 Relevance of the mandatory/discretionary distinction

171. In *Canada – Aircraft Credits and Guarantees*, Brazil claimed that certain Canadian programmes were "as such" prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement. The Panel considered that, as Brazil's claims regarded programmes as such, the mandatory/discretionary distinction "would traditionally apply", i.e., that only legislation that *requires* a violation of GATT/WTO rules could be found to be inconsistent with those rules:

"We recall that Brazil claims that the EDC Canada and Corporate Accounts and *IQ* are 'as such' prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement. Given that Brazil's claims are in respect of the programmes as such, the mandatory/discretionary distinction would traditionally apply. Under that distinction – employed in both GATT and WTO cases over the years – only legislation that requires a violation of GATT/WTO rules could be found to be inconsistent with those rules.

In this regard, we recall that the panel in *United States – Export Restraints* stated:

There is a considerable body of dispute settlement practice under both GATT and WTO standing for the principle that only legislation that *mandates* a violation of GATT/WTO obligations can be found as such to be inconsistent with those obligations. This principle was recently noted and applied by the Appellate Body in *United States – Anti-Dumping Act of 1916 ('1916 Act')*:

[T]he concept of mandatory as distinguished from discretionary legislation was developed by a number of GATT panels as a threshold consideration in determining when legislation as such – rather than a specific application of that legislation – was inconsistent with a Contracting Party's GATT 1947 obligations.

²⁵² Appellate Body Report, *Canada – Renewable Energy*, para. 5.188.

²⁵³ Appellate Body Report, *US – Lead and Bismuth II*, para. 12.

²⁵⁴ Appellate Body Report, *US – Lead and Bismuth II*, para. 60.

²⁵⁵ Appellate Body Report, *US – Lead and Bismuth II*, para. 62.

...

[P]anels developed the concept that mandatory and discretionary legislation should be distinguished from each other, reasoning that only legislation that mandates a violation of GATT obligations can be found as such to be inconsistent with those obligations."²⁵⁶

1.4.2.2.1.2 Order of analysis when applying the mandatory/discretionary distinction

172. The Panel in *Canada – Aircraft Credits and Guarantees* further explained that it would examine each of the programmes at issue to see if they mandated a benefit within the meaning of Article 1, and, if so, it would then examine whether that subsidy was contingent upon export performance.²⁵⁷ The Panel stressed:

"[W]e shall apply the mandatory/discretionary distinction in this dispute in determining whether the Canadian programmes at issue are as such inconsistent with WTO obligations, i. e., whether the legal texts governing the establishment and operation of these programmes are mandatory in respect of the violations alleged by Brazil. In other words, to assess Brazil's claim against the EDC as such, we must determine whether the EDC programme mandates the grant of prohibited export subsidies in a manner inconsistent with Article 3.1(a) of the SCM Agreement."²⁵⁸

1.4.2.2.1.3 "Substantive context" in the application of the mandatory/discretionary distinction

173. In *Canada – Aircraft Credits and Guarantees*, Brazil argued that the mandatory/discretionary distinction should be applied in the "substantive context" of the Canadian programme at issue further to the Panel report in *US – Export Restraints*.²⁵⁹ The Panel disagreed with Brazil's interpretation of the Panel report in that case and considered that the relevant "substantive context" in applying the mandatory/discretionary distinction would be the obligations set forth in Article 3.1(a) of the SCM Agreement, and not the programmes under review:

"We note, ... that the Panel in [*United States – Export Restraints*] was primarily addressing the issue of whether the mandatory/discretionary distinction had to be addressed by a panel as a threshold matter as argued by the United States in that case, or whether a panel could address this distinction after considering the legal requirements of the applicable provisions of the WTO Agreement. In other words, the phrase 'substantive context' refers to Articles 1 and 3 of the SCM Agreement, and not the measure under review. The point made by the panel in *United States – Export Restraints* is simply that it may be difficult to determine whether non-conforming conduct is mandated, without first determining what the obligations are against which conformity is measured. In the present case, the relevant 'substantive context' in applying the mandatory/discretionary distinction would be the obligations set forth in Article 3.1(a) of the SCM Agreement, and not the programmes under review.

We shall therefore apply the mandatory/discretionary distinction in light of Article 3.1(a) of the SCM Agreement. In other words, the question we must address is whether the EDC – the EDC Canada Account and the EDC Corporate Account – or *IQ* requires Canada to provide subsidies contingent upon export performance within the meaning of Article 3.1(a) of the SCM Agreement."²⁶⁰

1.4.2.2.1.4 Extent of the complainant's burden of proof

174. The Appellate Body in *Canada – Renewable Energy* considered a claim by the complainants that the Panel had erred in finding that the complainants had failed to establish that the

²⁵⁶ Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.56-7.57.

²⁵⁷ Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.56-7.59 and 7.68.

²⁵⁸ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.59.

²⁶⁰ Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.61-7.62.

challenged measures conferred a benefit. The Appellate Body stated that "[i]n making a *prima facie* case of benefit under Article 1.1(b) of the SCM Agreement, the burden was on the complainants to identify a suitable benchmark and to make adjustments, where necessary".²⁶¹

175. The Panel in *Canada – Aircraft Credits and Guarantees* considered that, to prove that a given programme "as such" provides export subsidies, the complainant must establish, on the basis of the pertinent legal instruments, that the programmes at issue "mandate subsidisation, in particular, the conferral of a benefit":

"Whatever the reason for the existence of export credit agencies, to prove that the EDC as such provides export subsidies, Brazil would have to establish that to be the case on the basis of the various legal texts regarding the establishment and operation of the EDC (i. e., both its Canada and its Corporate Accounts).

We consider that, despite the fact that Brazil has the burden of proof, it has not pointed to any specific provision in those legal texts that suggests that these programmes mandate subsidisation, in particular, the conferral of a benefit within the meaning of Article 1 of the SCM Agreement. We have nonetheless examined the various legal texts submitted by Brazil and found nothing that points to mandatory subsidisation on the part of the EDC."²⁶²

176. The Panel in *Canada – Aircraft Credits and Guarantees* clarified that "[t]o satisfy the 'benefit' element of Article 1.1 of the SCM Agreement for purposes of a challenge to [the programme at issue] as such, [the complainant] must show that the programme requires conferral of a benefit, not that it could be used to do so, or even that it is used to do so."²⁶³

177. The Panel in *Korea – Commercial Vessels* considered whether the KEXIM legal regime confers a "benefit" as such because the KEXIM Act imposes no obligation on KEXIM to take market conditions into account when disbursing funds. The Panel concluded that it does not:

"We do not consider that a legal instrument may be found to mandate subsidization simply because it neither prohibits subsidization nor requires market conditions to be taken into account. The fact that a legal instrument is silent on subsidization should not lead to a conclusion that the resultant discretion will of necessity be exercised in a manner that results in subsidization. As stated by the Appellate Body in *US – Section 211 Appropriations Act*, "where discretionary authority is vested in the executive branch of a WTO Member, it cannot be assumed that the WTO Member will fail to implement its obligations under the WTO Agreement in good faith".²⁶⁴²⁶⁵

178. The Panel in *Korea – Commercial Vessels* explained that although certain provisions of a legal instrument might indicate that it was intended as a means of providing subsidies "a conclusion that the [KLR] could be applied in a manner that confers a benefit would not be a sufficient basis to conclude that the KLR as such is mandatory legislation susceptible of inconsistency with Article 3.1(a) of the SCM Agreement."²⁶⁶²⁶⁷

Fiscal advantages

179. The Panel in *Canada – Aircraft Credits and Guarantees* clarified that the granting of fiscal advantages *per se* does not prove that the entity is required to pass on those advantages to its clients in the form of Article 1 subsidies and that even if the programme may have provided subsidies in the past, it does not then follow that the programme under consideration is *required* to provide such subsidies:

²⁶¹ Appellate Body Report, *Canada – Renewable Energy*, para. 5.216.

²⁶² Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.76-7.77.

²⁶³ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.107. See also paras. 7.123-7.125 and Panel Report, *Brazil – Aircraft (Article 21.5 – Canada II)*, paras. 5.43 and 5.50.

²⁶⁵ Panel Report, *Korea – Commercial Vessels*, para. 7.78.

²⁶⁷ Panel Report, *Korea – Commercial Vessels*, para. 7.107.

"Brazil submits that ECAs benefit from a competitive advantage over their private sector competitors (because ECAs do not pay taxes, for example), and this enables them to offer more favourable terms than those available in the private sector. According to Brazil, 'not paying taxes is illustrative of, and an essential prerequisite to, an ECA's capability to perform its normal mission – to provide export subsidies'. Brazil also implies that there would be no need for the EDC if it did not provide support on terms more favourable than those available on the market. Whether or not these arguments are factually correct, however, we do not see how they establish mandatory subsidization. That an entity enjoys certain fiscal advantages does not in and of itself prove that that entity is required to pass on those advantages to its clients in the form of subsidies within the meaning of Article 1 of the SCM Agreement.

In our opinion, the fact that ECAs may have a competitive advantage that allows them to undercut private sector competitors does not mean that they are necessarily required to do so. Furthermore, although the EDC may have provided subsidies in the form of loan guarantees, financial services or debt financing in specific transactions, it does not follow from this that the EDC is required to provide such subsidies."²⁶⁸

Compliance with the OECD Arrangement

180. The Panel in *Canada – Aircraft Credits and Guarantees* further considered that "[w]hile it may be true that even when a programme complies with the OECD Arrangement, it may – pursuant to the findings of the Panel in *Canada – Aircraft (Article 21.5 – Brazil)* involve the grant of prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement, that is not necessarily the case."²⁶⁹

Provision of services not available in the market

181. The Panel in *Canada – Aircraft Credits and Guarantees* rejected the complainant's argument that the programme provided a subsidy by providing services that were not available on the market and clarified that, even if the particular programme had the potential to offer such other services, that fact did not necessarily mean that it was required to do so:

"Even assuming that the provision of services not available on the market necessarily confers a benefit, the fact that the EDC Corporate Account has the 'ability' to provide such services does not necessarily mean that it is required to do so. As noted above, to satisfy the 'benefit' element of Article 1.1 of the SCM Agreement for purposes of a challenge to the EDC Corporate Account as such, Brazil would have to show that the program requires conferral of a benefit, not that it could be used to do so, or even that it is used to do so."²⁷⁰²⁷¹

1.4.2.2.1.5 Challenging subsidy programmes "as applied"

182. The Panel in *Canada – Aircraft Credits and Guarantees* considered it inappropriate to make a finding on the subsidies programmes under consideration "as applied" because the complainant's "as applied" claims were based on evidence from specific transactions, and these claims were not independent from claims regarding specific transactions for which the Panel did make findings. The Panel considered that "findings regarding a programme 'as applied' would undermine the utility of the mandatory/discretionary distinction":

²⁶⁸ Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.80-7.81.

²⁶⁹ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.93.

²⁷⁰ (footnote original) This is not a case where EDC Corporate Account support necessarily confers a benefit, and where the only discretion available is that of not providing the support at all. We do not express a view as to whether our approach in this case would be equally applicable in such factual circumstances. Rather, this is a case where Canada has discretion to operate the EDC Corporate Account in such a manner that it does not confer a benefit. Further, we note that the facts before us are unlike those before the Appellate Body in *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*. In that case, the Appellate Body was reviewing mandatory legislation. (See *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, Report of the Appellate Body, WT/DS56/AB/R, adopted 22 April 1998, paras. 49 and 54.)

²⁷¹ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.111.

"In our view, there are a number of reasons why it would not be appropriate for us to make separate findings regarding the EDC and IQ programmes 'as applied'. First, we do not consider that Brazil's 'as applied' claims are independent of its claims regarding 'specific transactions'. Indeed, Brazil itself acknowledges that '[i]n order for Brazil to prevail on its 'as applied' claims, the Panel must find that the challenged programmes have been *applied in specific transactions* in a manner that is inconsistent with the SCM Agreement'. Since Brazil's 'as applied' claims are not independent of its claims against 'specific transactions', and since we make findings regarding 'specific transactions', we see no practical purpose in making 'as applied' findings.

[W]e recall our earlier remarks regarding the application of the mandatory / discretionary distinction. Further, we recall the statement of the panel in *United States – Export Restraints* that 'the distinction between mandatory and discretionary legislation has a rational objective in ensuring predictability of conditions for trade. It allows parties to challenge measures that will necessarily result in action inconsistent with GATT/WTO obligations, *before* such action is actually taken'²⁷². The conclusion by a panel that a programme is discretionary and therefore is not inconsistent with the WTO Agreement and a subsequent conclusion, by the same panel, that the programme 'as applied' (i.e., the manner in which the discretion inherent in that programme has been applied) is inconsistent with the WTO Agreement would be of little value. In our view, findings regarding a programme 'as applied' would undermine the utility of the mandatory / discretionary distinction."²⁷³

1.4.3 Pass-through of benefit: changes in ownership

183. In *US – Lead and Bismuth II*, the European Communities challenged the administrative review of the imposition of countervailing duties by US authorities. The US investigating authorities had imposed countervailing duties on products of a company which had received subsidized equity infusions from the UK Government while still under state control, but for which a fair market value price had been paid in a subsequent privatization by the buyers. Both the equity infusion and the privatization had occurred prior to the initiation of the investigation of the US authorities. The applicable US statutory provisions contained an "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."²⁷⁴ As a consequence, the competent US authority examined whether "potentially allocable subsidies ... could have travelled with the productive unit" following a change in ownership and concluded that a benefit indeed still existed, accruing to the new owners of the privatized corporation. In its report, the Panel first found that, in general, there could not be an irrebuttable presumption that a benefit "continues to flow from untied, non-recurring 'financial contributions', even after changes in ownership."²⁷⁵ The Panel then stated that it also failed to see how, in the specific case at hand, the new owners of the producing facility could be deemed to have obtained a benefit by previous subsidies bestowed upon the enterprise, if a fair market value had been paid for all productive assets in the course of the privatization.²⁷⁶ Upon appeal, the Appellate Body held that it saw "no error in the Panel's conclusion".²⁷⁷

184. Discussing the payment of value by owners of companies, rather than the companies themselves, the Panel in *US – Lead and Bismuth II* held that "[i]n 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'".²⁷⁸

185. In *EC and certain member States – Large Civil Aircraft*, the Appellate Body reversed the Panel's finding that the sales transactions at issue did not "extinguish" a portion of past subsidies, because the Panel failed to assess whether the partial privatizations and private-to-private sales

²⁷³ Panel Report, *Canada – Aircraft Credits and Guarantees*, paras. 7.130 and 7.132.

²⁷⁴ Panel Report, *US – Lead and Bismuth II*, para. 6.59, quoting from the United States' submission.

²⁷⁵ Panel Report, *US – Lead and Bismuth II*, para. 6.71.

²⁷⁶ Panel Report, *US – Lead and Bismuth II*, para. 6.81.

²⁷⁷ Appellate Body Report, *US – Lead and Bismuth II*, para. 68.

²⁷⁸ Panel Report, *US – Lead and Bismuth II*, para. 6.82.

transactions were at arm's-length terms and for fair market value, and to what extent they involved a transfer in ownership and control to new owners. The Appellate Body found that there were insufficient factual findings by the Panel or undisputed facts on the Panel record to complete the legal analysis and determine whether these transactions "extinguished" a portion of past subsidies. The Appellate Body did not *a priori* exclude the possibility that all or part of a subsidy may be "extracted" by the removal of cash or cash equivalents, but upheld the Panel's ultimate finding that the "cash extractions" at issue in that case did not remove a portion of past subsidies. The Appellate Body upheld the Panel's ultimate finding that the "cash extractions" did not result in the "withdrawal" of subsidies within the meaning of Articles 4.7 and 7.8 of the SCM Agreement; and had no basis on which to make a finding that the sales transactions at issue resulted in the "withdrawal" of subsidies within the meaning of Articles 4.7 and 7.8 of the SCM Agreement.²⁷⁹

1.4.4 Pass-through of benefit: subsidized inputs

186. In *US – Softwood Lumber III*, the Panel, basing itself on the findings of the Appellate Body in *US – Lead and Bismuth II*²⁸⁰, examined whether considering the facts of this case, the Member conducting a countervailing duty investigation was required to examine if the alleged benefit to the *tenure holders* from the stumpage programmes were "passed through" to the *softwood lumber producers*.²⁸¹ In the Panel's view, an authority "may not assume that a subsidy provided to producers of the 'upstream' input product automatically benefits unrelated producers of downstream products, especially if there is evidence on the record of arm's-length transactions between the two." For the Panel, in such circumstances the investigating authority should "examine whether and to what extent the subsidies bestowed on the upstream producers benefited the downstream producers."²⁸²

187. The Panel in *US – Softwood Lumber III* concluded that where there is "complete identity between the tenure holder/logger and the lumber producer, no pass-through analysis is required." The Panel found that "where a downstream producer of subject merchandise is unrelated to the allegedly subsidized upstream producer of the input, an authority is not allowed to simply assume that a benefit has passed through." The Panel concluded that by "not examining whether the independent lumber producers 'paid arm's-length prices' for the logs that they purchased", the Member defined the benefit to the producers of the subject merchandise inconsistently with the SCM Agreement.²⁸³ There was no appeal in this case.

188. Pass-through in respect of subsidized inputs was also examined in *United States – Softwood Lumber IV*. Although the claims in that case were not brought under Article 1.1(b) of the SCM Agreement, the Appellate Body made the following remarks regarding the relevance of that provision to the broader issue at hand:

"This interpretation is also borne out by the general definition of a 'subsidy' in Article 1 of the *SCM Agreement*. According to that definition, a subsidy shall be deemed to exist only if there is both a *financial contribution* by a government within the meaning of Article 1.1(a)(1)²⁸⁴, and a *benefit* is thereby conferred within the meaning of Article 1.1(b).²⁸⁵ If countervailing duties are intended to offset a subsidy granted to the producer of an input product, but the duties are to be imposed on the *processed product* (and not the input product), it is *not* sufficient for an investigating authority to establish only for the *input* product the existence of a financial contribution and the conferral of a benefit to the input producer. In such a case, the cumulative conditions set out in Article 1 must be established with respect to the processed product, especially when the producers of the input and the processed product are not the same entity. The investigating authority must establish that a *financial contribution* exists; and it must also establish that the benefit resulting from the subsidy has passed through, at least in part, from the input downstream, so as to *benefit* indirectly the processed product to be countervailed.

²⁷⁹ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, paras. 718-749.

²⁸⁰ Appellate Body Report, *US – Lead and Bismuth II*, para. 68.

²⁸¹ Panel Report, *US – Softwood Lumber III*, paras. 7.68-7.69.

²⁸² Panel Report, *US – Softwood Lumber III*, para. 7.71.

²⁸³ Panel Report, *US – Softwood Lumber III*, paras. 7.72 and 7.74.

²⁸⁴ (footnote original) Or income or price support within the meaning of Article 1.1(a)(2).

In this respect, the Appellate Body's interpretation of the term 'benefit' in *Canada – Aircraft* is useful:

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.²⁸⁶

Thus, for a potentially countervailable subsidy to exist, there must be a financial contribution by the government that confers a benefit to a *recipient*. Where a subsidy is conferred on input products, and the countervailing duty is imposed on processed products, the initial recipient of the subsidy and the producer of the eventually countervailed product, may not be the same. In such a case, there is a *direct recipient* of the benefit—the producer of the *input* product. When the input is subsequently processed, the producer of the *processed product* is an *indirect recipient* of the benefit—provided it can be established that the benefit flowing from the input subsidy is passed through, at least in part, to the processed product. Where the input producers and producers of the processed products operate at *arm's length*, the pass-through of input subsidy benefits from the direct recipients to the indirect recipients downstream cannot simply be presumed; it must be established by the investigating authority. In the absence of such analysis, it cannot be shown that the essential elements of the subsidy definition in Article 1 are present in respect of the *processed product*. In turn, the right to impose a countervailing duty on the processed product for the purpose of offsetting an input subsidy, would not have been established in accordance with Article VI:3 of the GATT 1994, and, consequently, would also not have been in accordance with Articles 10 and 32.1 of the *SCM Agreement*.²⁸⁷

1.4.5 Pass-through: sales of the subsidized product to unrelated buyers

189. In *Mexico – Olive Oil*, the European Communities relied on the findings of the Appellate Body in *US – Softwood Lumber IV* regarding "pass-through" to claim that, pursuant to Article 1.1(b), Mexico should have conducted a pass-through analysis to determine whether any of the subsidy benefit conferred on olive growers was transmitted to the unrelated exporters of olive oil to Mexico. The Panel rejected the European Communities' claim. The Panel distinguished *US – Softwood Lumber IV*, since the case before the Panel did not involve the use of inputs (e.g., olives) not covered by the investigation in the production of the product subject to the investigation (i.e., olive oil). Rather, the transactions referred to by the European Communities all involved the investigated product (i.e., olive oil). The Panel found that a pass-through analysis was not required when the product under investigation was sold prior to exportation, even if the sale involved unrelated parties:

"The *US – Softwood Lumber IV* and *US – Canadian Pork* jurisprudence does *not* support the European Communities' argument that whenever there is *any* arms'-length transaction between unrelated companies in the chain of the production of an imported product subject to a countervail investigation, a pass-through analysis must be conducted. To the contrary, as discussed above, in *US – Softwood Lumber IV*, the Appellate Body found that where an input product and a further manufactured product *both* are covered by the definition of the product subject to the countervailing duty investigation, a pass-through analysis is *not* required even if the producers of the respective products are *unrelated* and operating at arms' length. If this is the case for certain arms'-length sales of *inputs* between unrelated firms, then *a fortiori* the mere existence of an arms'-length transaction between firms involving the product under investigation somewhere between the receipt of the subsidy and the export of the merchandise should not, by itself, give rise to an obligation to conduct a pass-through analysis under Article VI:3 of the GATT 1994 and Article 10 of the *SCM Agreement*.

In this respect, we recall that the *SCM Agreement* and Article VI:3 of the GATT 1994 both explicitly permit the application of countervailing measures to 'offset' subsidies

²⁸⁷ Appellate Body Report, *US – Softwood Lumber IV*, paras. 142-143.

'bestowed upon [...] *the manufacture, production or export* ' of a product (emphasis added). Taking the simplest hypothetical example, where a subsidy is provided directly to a producer of a product coming within the scope of a countervailing duty investigation, we do not see how that company's eventual sale of the product to an unrelated firm (e.g., a distributor) would have a bearing on the fact that a subsidy has been bestowed in respect of the 'production ' of that product. Taken to its logical conclusion, the argument by the European Communities, that a pass-through analysis must be conducted in every case in which there are transactions between unrelated firms relating to the product under investigation, would mean that a pass-through analysis would be required in almost every countervail investigation, even when the subsidy was provided directly on the investigated product."²⁸⁸

190. Turning to the specifics of the European Communities' claim, the Panel first noted that, whereas the findings of the Appellate Body in *US – Softwood Lumber IV* were based on Article 10 of the SCM Agreement and Article VI:3 of the GATT 1994, the European Communities' claim was based *inter alia* on Article 1.1(b) of the SCM Agreement. The Panel then noted that the European Communities did not argue that a benefit was not conferred in respect of exports of olive oil to Mexico. Rather, the European Communities argued that Mexico did not properly calculate the amount of the benefit that was directly attached to the exports of olive oil. The Panel rejected the European Communities' argument on the basis that Article 1.1(b) "in itself does not establish a requirement to calculate precisely the amount of the benefit accruing to a particular recipient in a countervail investigation".²⁸⁹

1.4.6 Rebuttal of a prima facie case of benefit

191. Considering whether a party has rebutted a prima facie case of subsidization established against it, the Panel in *Canada – Aircraft* stated:

"In order to rebut the *prima facie* case of 'benefit', we consider that Canada must do more than simply demonstrate that the amount of specific 'benefit' estimated by Brazil may be incorrect, or that TPC's rate of return covers Canada's cost of funds. Rather, Canada must demonstrate that no 'benefit' is conferred, in the sense that the terms of the contribution provide for a commercial rate of return."²⁹⁰

192. In *Canada – Aircraft Credits and Guarantees*, the Panel noted the statements made by a Member's government official that the programme financing under consideration would be at a "better rate" than loans available commercially. For the Panel, these statements were an indication that the financing confers a "benefit":

"We recall that a 'benefit' is conferred when a recipient receives a 'financial contribution' on terms more favourable than those available to the recipient in the market. In our view, Minister Tobin's statements indicate that the Canada Account financing to Air Wisconsin, which will take the form of a loan, will confer a 'benefit' because it will be on terms more favourable than those available to the recipient in the market. This is confirmed by the fact that, in these proceedings, Canada itself initially considered the terms of the Canada Account financing to Air Wisconsin to be more favourable than those available in the market."²⁹¹

1.4.7 Relationship with other provisions of the SCM Agreement

1.4.7.1 Article 14

193. Both the Panel and the Appellate Body in *Canada – Aircraft* held that Article 14 was relevant context for interpretation of the term "benefit". The Appellate Body considered the explicit reference to Article 1.1 contained in Article 14:

²⁸⁸ Panel Report, *Mexico – Olive Oil*, paras. 7.143-7.144.

²⁸⁹ Panel Report, *Mexico – Olive Oil*, para. 7.152.

²⁹⁰ Panel Report, *Canada – Aircraft*, para. 9.312.

²⁹¹ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.144.

"Although the opening words of Article 14 state that the guidelines it establishes apply '[f]or the purposes of Part V' of the *SCM Agreement*, which relates to 'countervailing measures', our view is that Article 14, nonetheless, constitutes relevant context for the interpretation of 'benefit' in Article 1.1(b). The guidelines set forth in Article 14 apply to the calculation of the 'benefit to the recipient conferred pursuant to paragraph 1 of Article 1'. (emphasis added) This explicit textual reference to Article 1.1 in Article 14 indicates to us that 'benefit' is used in the same sense in Article 14 as it is in Article 1.1. Therefore, the reference to 'benefit to the recipient' in Article 14 also implies that the word 'benefit', as used in Article 1.1, is concerned with the 'benefit to the recipient' and not with the 'cost to government'.

...

Article 14, which we have said is relevant context in interpreting Article 1.1(b), supports our view that the marketplace is an appropriate basis for comparison. The guidelines set forth in Article 14 relate to equity investments, loans, loan guarantees, the provision of goods or services by a government, and the purchase of goods by a government. A 'benefit' arises under each of the guidelines if the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market."²⁹²

194. In *Canada – Renewable Energy*, the Appellate Body noted that it had relied on Article 14 as relevant context for the interpretation of benefit under Article 1.1(b) in previous disputes under both Parts II and III of the SCM Agreement. Moreover, it addressed the place of Article 14 in the SCM Agreement:

"Although Article 14 is in Part V of the SCM Agreement, the Panel was correct in pointing out that it is relevant context to the interpretation of Article 1.1(b) for the purpose of Part II of the SCM Agreement, and that it can be used as relevant context to determine whether a subsidy exists."²⁹³

195. Moreover, in *Canada – Renewable Energy*, the Appellate Body considered that the determination of the mere existence, as opposed to the amount, of a subsidy does not require a different approach to determining benefit under Article 1.1(b):

"We do not think that a different approach should be adopted when, as in the case of prohibited subsidies, one has to determine whether a benefit exists as opposed to its precise quantification. A market benchmark can tell us whether a benefit exists and usually its size. However, in the absence of a market benchmark, it will not be possible to establish if a subsidy exists at all. That a financial contribution confers an advantage on its recipient cannot be determined in absolute terms, but requires a comparison with a benchmark, which, in the case of subsidies, derives from the market. This is so, in our view, regardless of whether the advantage needs to be precisely quantified or not."²⁹⁴

196. In *Canada – Renewable Energy*, the Appellate Body concluded that "[a] determination of the existence of a benefit under Article 1.1(b), read in the context of Article 14(d) of the SCM Agreement, requires a comparison between actual remuneration and a market-based benchmark or proxy, and thus between amounts, in order to determine the existence of a benefit".²⁹⁵

1.4.7.2 Article 14(c)

197. With regard to establishing the existence of a benefit relating to equity guarantees in the framework of the SCM Agreement, the Panel in *Canada – Aircraft Credits and Guarantees*, noted the relevance of Article 14(c). Accordingly, it considered that a "benefit" could arise if there is a difference between the cost of equity with and without an equity guarantee programme, provided

²⁹² Appellate Body Report, *Canada – Aircraft*, paras. 155 and 158.

²⁹³ Appellate Body Report, *Canada – Renewable Energy*, para. 5.163.

²⁹⁴ Appellate Body Report, *Canada – Renewable Energy*, para. 5.164.

²⁹⁵ Appellate Body Report, *Canada – Renewable Energy*, para. 5.165.

that such difference is not topped by the fees charged by the programme for providing the equity guarantee.²⁹⁶

1.4.7.3 Article 14(d)

198. In relation to the context provided by Article 14 for the interpretation of "benefit" under Article 1.1(b), the Appellate Body in *Canada – Renewable Energy* stated that "Article 14(d) contains guidelines for determining whether government purchases of goods make a recipient 'better off' than it would otherwise be in the marketplace".²⁹⁷

199. In *Canada – Renewable Energy*, the Appellate Body stated that a "benefit analysis under Article 1.1(b), read in the context of Article 14(d) of the SCM Agreement, involves a comparison with a market benchmark or proxy".²⁹⁸ The Appellate Body further explained:

"Article 14(d) states, on the one hand, that purchases of goods should be considered as conferring a benefit if 'the purchase is made for more than adequate remuneration' and, on the other hand, that the adequacy of remuneration has to be determined in relation to the 'prevailing market conditions' for the good or service in question in the country of purchase. The adequacy of remuneration is only one aspect of the Article 14(d) comparison, the other being the 'prevailing *market* conditions' in the country of purchase, which requires a comparison with a market benchmark.

That Article 14(d) requires a comparison with *market* conditions was confirmed by the Appellate Body in *US – Softwood Lumber IV*. The Appellate Body found that, in cases where the private prices of the goods in question in the country of provision are distorted, it is possible to resort to an out-of-country benchmark or to a constructed benchmark, provided that the necessary adjustments are made to reflect conditions in the market of purchase. The very purpose of resorting to an out-of-country or to a constructed benchmark is to replicate competitive market conditions that are absent in the country of purchase. Thus, resorting to a benchmark that does not reflect market conditions would not be consistent with the guidelines of Article 14(d), as interpreted by the Appellate Body in *US – Softwood Lumber IV*.²⁹⁹

1.4.7.4 Annex I, item (k)

200. The Panel in *Canada – Aircraft* rejected the use of item (k) in the interpretation of the term "benefit". The Panel noted:

"[W]e are unable to accept ... [the] argument that item (k) of the Illustrative List of Annex I of the SCM Agreement constitutes contextual guidance for determining the existence of 'benefit' in the specific context of government credit under Article 1. In our view, item (k) of the Illustrative List applies in determining whether or not a prohibited export subsidy exists. We do not consider ... that item (k) determines whether or not a 'subsidy' exists within the meaning of Article 1 of the SCM Agreement."³⁰⁰

201. In *Brazil – Aircraft*, the Appellate Body rejected the Panel's interpretation of the "material advantage" clause in item (k) of the Illustrative List of Export Subsidies as effectively the same interpretation of the term "benefit" in Article 1.1(b) adopted by the Panel in *Canada – Aircraft*.³⁰¹

1.4.7.5 Annex IV

202. The Appellate Body in *Canada – Aircraft* agreed with the Panel "that Annex IV is not useful context for interpreting Article 1.1(b)"³⁰², stating:

²⁹⁶ Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.345.

²⁹⁷ Appellate Body Report, *Canada – Renewable Energy*, para. 5.163.

²⁹⁸ Appellate Body Report, *Canada – Renewable Energy*, para. 5.183. See also Appellate Body Report, *US – Countervailing Measures (China)*, para. 4.44.

²⁹⁹ Appellate Body Report, *Canada – Renewable Energy*, paras. 5.183-5.184.

³⁰⁰ Panel Report, *Canada – Aircraft*, para. 9.117.

³⁰¹ Appellate Body Report, *Brazil – Aircraft*, para. 179.

"We fail to see the relevance of this provision to the interpretation of 'benefit' in Article 1.1(b) of the *SCM Agreement*. Annex IV provides a method for calculating the total *ad valorem* subsidization of a product under the 'serious prejudice' provisions of Article 6 of the *SCM Agreement*, with a view to determining whether a subsidy is used in such a manner as to have 'adverse effects'. Annex IV, therefore, has nothing to do with whether a 'benefit' has been conferred, nor with whether a measure constitutes a subsidy within the meaning of Article 1.1."³⁰³

1.4.8 Relationship with other Agreements

1.4.8.1 TRIMs Agreement

203. In *Canada – Renewable Energy*, the Appellate Body addressed the relationship between the interpretations of "benefit" under Article 1.1(b) of the SCM Agreement and "advantage" under the TRIMs Agreement:

"In *Canada – Aircraft* and in its later jurisprudence, the Appellate Body did not equate the notions of 'benefit' and 'advantage'. The Appellate Body's interpretation of 'benefit' in Article 1.1(b) of the SCM Agreement clearly suggests that, while benefit involves some form of advantage, the former has a more specific meaning under the SCM Agreement. 'Benefit' is linked to the concepts of 'financial contribution' and 'income or price support', and its existence requires a comparison in the marketplace. The same cannot be said about an 'advantage' within the meaning of the TRIMs Agreement. Paragraph 1 of the Illustrative List of the TRIMs Agreement simply refers to TRIMs that are necessary to obtain an advantage. The concept of 'advantage' in the TRIMs Agreement has to be interpreted in the context of this Agreement and, without entering into the merit of such an interpretation, it seems to us that 'advantage' under the TRIMs Agreement may take other forms than a 'financial contribution' or a 'benefit' under the SCM Agreement. In any event, a finding of an 'advantage' under the TRIMs Agreement does not require a comparison with a benefit benchmark in the relevant market, as required for a benefit analysis under the SCM Agreement.

Thus, while we do not exclude that certain measures that provide an advantage within the meaning of paragraph 1 of the Illustrative List of the TRIMs Agreement may also confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement, it is conceivable that a measure that confers an advantage within the meaning of paragraph 1 of the Illustrative List of the TRIMs Agreement be found not to confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement."³⁰⁴

1.5 Relationship of Article 1.1 with other provisions of the SCM Agreement

1.5.1 Footnote 1 and Footnote 59

204. The Appellate Body in *US – FSC* rejected the argument that footnote 59 to the SCM Agreement, rather than Article 1.1, was the "controlling legal provision" for the definition of the term "subsidy". In doing so, the Appellate Body distinguished between the general definition of the term "subsidy" under Article 1.1 and the specific regime which footnote 59 establishes with respect to a certain type of *export* subsidies:

"Article 1.1 sets forth the general definition of the term 'subsidy' which applies 'for the purpose of this Agreement'. This definition, therefore, applies wherever the word 'subsidy' occurs throughout the *SCM Agreement* and conditions the application of the provisions of that Agreement regarding *prohibited* subsidies in Part II, *actionable* subsidies in Part III, *non-actionable* subsidies in Part IV and countervailing measures in Part V. By contrast, footnote 59 relates to one item in the Illustrative List of Export Subsidies. Even if footnote 59 means – as the United States also argues – that a measure, such as the FSC measure, is *not* a prohibited *export* subsidy, footnote 59

³⁰² Appellate Body Report, *Canada – Aircraft*, para. 159.

³⁰³ Appellate Body Report, *Canada – Aircraft*, para. 159.

³⁰⁴ Appellate Body Report, *Canada – Renewable Energy*, paras. 5.208-5.209.

does not purport to establish an exception to the general definition of a '*subsidy*' otherwise applicable throughout the entire *SCM Agreement*. Under footnote 5 of the *SCM Agreement*, where the Illustrative List indicates that a measure is not a prohibited *export* subsidy, that measure is *not* deemed, for that reason alone, not to be a '*subsidy*'. Rather, the measure is simply *not prohibited* under the Agreement. Other provisions of the *SCM Agreement* may, however, still apply to such a '*subsidy*'.³⁰⁵

205. After distinguishing between the general definition of a subsidy under Article 1.1 and the special regime applicable to a *particular type of export* subsidy pursuant to footnote 59, the Appellate Body in *US – FSC* opined that footnote 1 of the *SCM Agreement* was equally not relevant in the case at hand, given that the United States' measure at issue provided for exemptions from *corporate income* taxes:

"We note, moreover, that, under footnote 1 of the *SCM Agreement*, 'the exemption of an exported *product* from duties or taxes *borne by the like product* when destined for domestic consumption ... shall not be deemed to be a subsidy'. (emphasis added) The tax measures identified in footnote 1 as not constituting a '*subsidy*' involve the exemption of exported *products* from *product-based* consumption taxes. The tax exemptions under the FSC measure relate to the taxation of *corporations* and not *products*. Footnote 1, therefore, does *not* cover measures such as the FSC measure."³⁰⁶

1.6 Relationship of Article 1.1 with other WTO Agreements

1.6.1 Article XVI of the WTO Agreement

206. The Appellate Body in *US – FSC* upheld the Panel's finding on whether the term "otherwise due" must be interpreted in accordance with the 1981 Understanding adopted by the GATT Council in conjunction with four panel reports on tax legislation, but modified the reasoning.³⁰⁷ First, the Appellate Body examined and confirmed the Panel's finding that the 1981 Council action is not part of the GATT 1994; in so doing, the Appellate Body considered whether the Council action is "another decision" within the meaning of paragraph 1(b)(iv) of the language incorporating the GATT 1994 into the WTO Agreement. The Appellate Body rejected this claim, recalling its holding in *Japan – Alcoholic Beverages* that GATT Panel reports are only binding as between the parties to the dispute; nevertheless, in the specific case at hand, it noted a certain ambiguity in this regard:

"The opening clause of the 1981 Council action states: 'The Council adopts *these reports* on the understanding that *with respect to these cases, and in general* ...'. The 1981 Council action is, therefore, somewhat equivocal in tenor. On the one hand, it is clear from the text that the 1981 Council action relates specifically to the *Tax Legislation Cases* and is an integral part of the resolution of those disputes. This would suggest that, consistently with our Report in *Japan – Alcoholic Beverages*, the Council action is binding only on the parties to those disputes, and only for the purposes of those disputes.

On the other hand, we note that the opening clause of the 1981 Council action also prefaces the substance of the statement with the words '*in general*'. The United States argues that these words indicate that the 1981 Council action was an 'authoritative interpretation' of Article XVI:4 of the GATT 1947 that has 'general' application and that, therefore, bound all the contracting parties. ...

...

[However,] [w]hen the 1981 Council action was adopted, the Chairman of the GATT 1947 Council stated, *inter alia*, that 'the adoption of these reports together with the understanding *does not affect the rights and obligations of contracting parties under the General Agreement*.' In our view, if the contracting parties had intended to

³⁰⁵ Appellate Body Report, *US – FSC*, para. 93.

³⁰⁶ Appellate Body Report, *US – FSC*, para. 93.

³⁰⁷ Panel Report, *US – FSC*, para. 7.85.

make an *authoritative* interpretation of Article XVI:4 of the GATT 1947, binding on all contracting parties, they would have said so in reasonably recognizable terms. ... Thus, we are of the view that the statement of the GATT 1947 Council Chairman is consistent with a reading of the 1981 Council action which views that action as an integral part of the resolution of the *Tax Legislation Cases*, binding only the parties to those disputes."³⁰⁸

207. After upholding the Panel's finding that the 1981 Council action did not represent another decision within the meaning of Article 1(b)(iv) of the language incorporating GATT 1994 into the WTO Agreements, the Appellate Body in *US – FSC* proceeded to examine the status of the 1981 Council action as a "decision" within the meaning of Article XVI:1 of the WTO Agreement. In doing so, the Appellate Body addressed the relationship between Article XVI:4 of the GATT 1994 and Articles 1.1(a)(1) and 3.1(a) of the SCM Agreement:

"We recognize that, as 'decisions' within the meaning of Article XVI:1 of the *WTO Agreement*, the adopted panel reports in the *Tax Legislation Cases*, together with the 1981 Council action, could provide 'guidance' to the WTO. ...

...

[T]he provisions of the *SCM Agreement* do not provide explicit assistance as to the relationship between the export subsidy provisions of the *SCM Agreement* and Article XVI:4 of the GATT 1994. In the absence of any such specific textual guidance, we must determine the relationship between Articles 1.1(a)(1) and 3.1(a) of the *SCM Agreement* and Article XVI:4 of the GATT 1994 on the basis of the texts of the relevant provisions as a whole. It is clear from even a cursory examination of Article XVI:4 of the GATT 1994 that it differs very substantially from the subsidy provisions of the *SCM Agreement*, and, in particular, from the export subsidy provisions of both the *SCM Agreement* and the *Agreement on Agriculture*. First of all, the *SCM Agreement* contains an express definition of the term 'subsidy' which is not contained in Article XVI:4. In fact, as we have observed previously, the *SCM Agreement* contains a broad package of new export subsidy disciplines that 'go well beyond merely applying and interpreting Articles VI, XVI and XXIII of the GATT 1947'. Next, Article XVI:4 prohibits export subsidies only when they result in the export sale of a product at a price lower than the 'comparable price charged for the like product to buyers in the domestic market.' In contrast, the *SCM Agreement* establishes a much broader prohibition against *any* subsidy which is 'contingent upon export performance'. To say the least, the rule contained in Article 3.1(a) of the *SCM Agreement* that all subsidies which are 'contingent upon export performance' are prohibited is significantly different from a rule that prohibits only those subsidies which result in a lower price for the exported product than the comparable price for that product when sold in the domestic market. Thus, whether or not a measure is an export subsidy under Article XVI:4 of the GATT 1947 provides no guidance in determining whether that measure is a prohibited export subsidy under Article 3.1(a) of the *SCM Agreement*. Also, and significantly, Article XVI:4 of the GATT 1994 does not apply to 'primary products', which include agricultural products. Unquestionably, the explicit export subsidy disciplines, relating to agricultural products, contained in Articles 3, 8, 9 and 10 of the *Agreement on Agriculture* must clearly take precedence over the *exemption* of primary products from export subsidy disciplines in Article XVI:4 of the GATT 1994.

Furthermore, as the Panel observed, the text of the 1981 Council action itself contains reference only to Article XVI:4, and the Chairman of the GATT 1947 Council stated expressly that the 1981 Council action did *not* affect the *Tokyo Round Subsidies Code*. We share the Panel's view that, in these circumstances, it would be incongruous to extend the scope of the action, beyond that intended, to the *SCM Agreement*. If the 1981 Council action did not affect the *Tokyo Round Subsidies Code*, which existed in

³⁰⁸ Appellate Body Report, *US – FSC*, paras. 109-110, and 112.

1981, it is difficult to see how that action could be seen to affect the *SCM Agreement*, which did not."³⁰⁹

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³⁰⁹ Appellate Body Report, *US – FSC*, paras. 115 and 117-118.