# *EUROPEAN UNION – COUNTERVAILING MEASURES ON CERTAIN POLYETHYLENE TEREPHTHALATE FROM PAKISTAN*

**(AB-2017-5 / DS486)**

**THIRD PARTICIPANT SUBMISSION OF THE UNITED STATES OF AMERICA**

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**SERVICE LIST**

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## I. INTRODUCTION

1. The United States welcomes the opportunity to present its views on certain findings raised on appeal by the European Union ("EU") and Pakistan. In this submission, the United States will present its views on the proper legal interpretation of certain provisions of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU"), the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement"), and the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994") that are relevant to this dispute.

2. The United States will address two issues. First, the United States will address the EU's claim that the Panel erred in considering an expired measure.[1] The Panel correctly decided to make findings on the EU measure, despite its expiration after the establishment of the Panel.[2] Because the Panel made a finding that the EU measure was inconsistent with its obligations under the SCM Agreement, however, the Panel had an obligation under Article 19.1 of the DSU to make a recommendation with respect to that finding of inconsistency. Therefore, if the Appellate Body upholds the Panel's findings of inconsistency under the SCM Agreement, it must recommend that the EU bring its measure into compliance with those obligations unless the parties agree that not issuing a recommendation will assist them in securing a positive resolution to this dispute.

3. Second, the United States will address the EU's claim that the Panel erred in finding that the EU measure was inconsistent with its obligations under the SCM Agreement.[3] In examining whether Pakistan's remission of excess duties under a duty drawback scheme constituted a financial contribution, the Panel misconstrued the applicable provisions and in doing so, reached a conclusion that is not supported by the text of the SCM Agreement.

## II. THE EUROPEAN UNION'S CLAIM THAT THE PANEL ERRED IN CONSIDERING EXPIRED MEASURES

4. The EU argues that the Panel erred in making findings on the contested measure because the measure expired on September 30, 2015, thereby ceasing to have any legal effects.[4] The EU's claim on appeal is that the Panel disregarded its basic obligations under Article 11 of the DSU, as informed by Article 3 of the DSU, when it proceeded to make findings on an expired measure.[5] The United States disagrees. As we discuss below, the expiration of a measure after panel establishment is not relevant to the Panel's analysis of WTO consistency, nor to its obligation under the DSU to make recommendations with respect to any measures found to be inconsistent with a Member's obligations.

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[1] *See* Appellant Submission by the European Union ("EU Appellant Submission"), paras. 23-53.

[2] *See* Report of the Panel, para. 7.13.

[3] *See* EU Appellant Submission, paras. 54-83.

[4] *See* EU Appellant Submission, para. 23.

[5] *See* EU Appellant Submission, para. 24; *see also id.*, para. 53 ("the European Union requests the Appellate Body to *reverse* the Panel's findings and conclusions contained in its report . . . and to *declare* them moot and with no legal effect.").

## A. Panel Findings Regarding the Expiration of the EU Measure

5. First, we briefly recall the findings of the Panel with respect to this issue. The Panel was established on March 25, 2015.[6] On March 3, 2016, the EU filed a request for a preliminary ruling. The request asked the Panel to: (a) cease all work on this dispute because the relevant EU countervailing duty (CVD) measures on certain polyethylene terephthalate (PET) from Pakistan terminated on September 30, 2015 (Termination Request); and (b) if the Panel denied the Termination Request, find that certain of Pakistan's claims are outside the Panel's terms of reference under the standards set forth in Article 6.2 of the DSU.[7]

6. In its report, the Panel took note of the expiry of the challenged measure and considered whether to proceed with making findings as to that measure.[8] The Panel determined to proceed and found that the challenged measure was not consistent with the EU's obligations under the covered agreements.[9]

7. As the Panel report states at paragraph 7.13:

> 7.13 . . . . The challenged measures have thus expired and ceased to have legal effect.[32] WTO panel and Appellate Body jurisprudence indicates that panels have discretion regarding whether to make findings regarding such expired measures.[33] We have not identified any reason to depart from this current of jurisprudence. We therefore have discretion as to whether to make findings with respect to the challenged measures in this dispute.
>
> [33] It is therefore possible neither: (a) for the European Union to "withdraw" the challenged measures . . . nor (b) for the Panel to issue meaningful recommendations under Article 19.1 of the DSU . . . . We emphasize the fact-specific nature of these conclusions. Given the array of measures subject to WTO dispute settlement . . . there may be other cases where it is unclear the extent to which the legal effect of a certain measure . . . expired in a manner that makes Article 19.1 recommendations inutile.

8. The Panel then proceeded to analyze the EU measure and ultimately reach a finding of inconsistency. The Panel did not make recommendations with respect to its finding. Without addressing the text of Article 19.1, the Panel concluded by stating: "[g]iven that the measures at issue in this dispute have expired, we make no recommendation to the DSB pursuant to Article 19.1 of the DSU."[10]

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[6] DSB, Minutes of the meeting held on 25 March 2015, (circulated on 1 May 2015), WT/DSB/M/359.

[7] *See* Panel Report, para. 7.9.

[8] *See* Panel Report, para. 7.13.

[9] *See* Panel Report, para. 7.13.

[10] Panel Report, para. 8.13.

### B. The Panel was Correct to Make Findings on a Measure Found to Be in Force at the Time of Panel Establishment

9. Contrary to what the EU claims in its appeal, the expiration of the measure was not relevant to the matter being examined by the Panel.

10. A panel's terms of reference are set out in Articles 7.1 and 6.2 of the DSU. Specifically, when the Dispute Settlement Body ("DSB") establishes a panel, the panel's terms of reference under Article 7.1 are (unless otherwise decided) "[t]o examine . . . the matter referred to the DSB" by the complainant in its panel request.[11] Under DSU Article 6.2, the "matter" to be examined by the DSB consists of "the specific measures at issue" and "a brief summary of the legal basis of the complaint."[12] As the Appellate Body recognized in *EC – Chicken Cuts*, "[t]he term 'specific measures at issue' in Article 6.2 suggests that, as a general rule, the measures included in a panel's terms of reference must be measures that are in existence at the time of the establishment of the panel."[13]

11. In *EC – Selected Customs Matters*, the panel and Appellate Body were presented with the question of what legal situation a panel is called upon, under Article 7.1 of the DSU, to examine. The panel and Appellate Body both concluded that, under the DSU, the task of a panel is to determine whether the measure at issue is consistent with the relevant obligations "*at the time of establishment of the Panel.*"[14] It is thus the challenged measures, as they existed at the time of the panel's establishment, when the "matter" was referred to the panel, that are properly within the panel's terms of reference and on which the panel should make findings.

12. The DSU addresses the role and duties of a panel with respect to the matter referred to it by the DSB. Specifically, Article 11 requires that the panel should make an objective assessment of the "matter", including an objective examination of the facts and the applicability of and conformity with the covered agreements.[15] The panel also must issue a report under Article 12.7 setting out its "findings of fact, the applicability of relevant provisions and the basic rationale" for those findings.[16]

13. Therefore, the panel in this dispute was authorized and charged by the DSU to make a finding with respect to the measures within its terms of reference found to be WTO-inconsistent, i.e., the challenged measures, as they existed at the time of the Panel's establishment. The expiration or withdrawal of one of the legal instruments identified in Pakistan's panel request

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[11] DSU, Art. 7.1.

[12] DSU, Art. 6.2; *see US – Carbon Steel (AB)*, para. 125; *Guatemala – Cement I (AB)*, para. 72.

[13] *EC – Chicken Cuts (AB)*, para. 156.

[14] *See, e.g., EC – Selected Customs Matters (AB)*, para. 187 (finding that the panel's review of the consistency of the challenged measure with the covered agreements properly should "have focused on these legal instruments as they existed and were administered at the time of establishment of the Panel"); *id*., para. 259 (finding the panel had not erred in declining to consider three exhibits, which concerned a regulation enacted after panel establishment, because although they "might have arguably supported the view that uniform administration had been achieved by the time the Panel Report was issued, we fail to see how [they] showed uniform administration at the time of the establishment of the Panel"); *see also EC – Approval and Marketing of Biotech Products*, para. 7.456.

[15] DSU, Art. 11.

[16] DSU, Art. 12.7.

does not alter the scope of the Panel's terms of reference, nor the Panel's mandate under the DSU. The United States thus agrees with Pakistan that the Panel acted in accordance with its obligations under the DSU by making findings with respect to the EU's measure, notwithstanding the expiry of that measure.[17]

14. Other panels and the Appellate Body have reached similar conclusions.[18] For example, in *China – Raw Materials*, the complainants challenged "export duties" and "export quotas" "comprised of basic framework legislation and implementing regulations . . . and specific measures . . . [issued] on an annual or time-bound basis."[19] As the three co-complainants requested, the panel made findings on the measures as they existed at the time of the panel's establishment and, with respect to measures found to be WTO-inconsistent, made a recommendation under Article 19.1 of the DSU. The Appellate Body found that the panel had acted correctly.[20]

15. Therefore, the United States considers the Panel's making of findings on the contested measure to be consistent with the requirements of the DSU, as the measure falls within the terms of reference that were set when the Panel was established.

### C. Where a Measure Is Found to Be Inconsistent with a WTO Agreement, a Panel or the Appellate Body Must Make a Recommendation Under Article 19.1 of the DSU

16. Article 19.1 of the DSU requires panels and the Appellate Body to make recommendations with respect to the measure found to be inconsistent with the WTO Agreements.

17. Pursuant to DSU Article 11, a panel's "function" is to assist the DSB by "mak[ing] an objective assessment of the matter before it, including . . . the applicability of and conformity with the relevant covered agreements." With respect to the panel's recommendation, Article 19.1 sets out in mandatory terms that, where a panel "concludes that a measure is inconsistent with a covered agreement, it *shall recommend* that the Member concerned bring *the measure* into conformity with that agreement."[21] Thus, pursuant to Article 19.1, a panel is *required* to make a

[17] *See* Pakistan Appellee Submission, para. 3.19.

[18] *See, e.g.*, *EC – IT Products*, para. 7.167 ("[W]e note that any repeal would have taken place after the panel was established and its terms of reference were set. Therefore, the Panel considers that it may make recommendations with respect to these measures."); *US – Wool Shirts and Blouses (Panel)*, para. 6.2 ("In the absence of an agreement between the parties to terminate the proceedings, we think that it is appropriate to issue our final report regarding the matter set out in the terms of reference of this Panel in order to comply with our mandate . . . notwithstanding the withdrawal of the US restraint."); *see also Indonesia – Autos*, para. 14.9; *Dominican Republic – Imports and Sale of Cigarettes (Panel)*, para. 7.344; *EC – Approval and Marketing of Biotech Products*, para. 7.456; *China – Raw Materials (AB)*, para. 260.

[19] *China – Raw Materials (AB)*, para. 264.

[20] *See China – Raw Materials (AB)*, para. 260 ("While a finding by a panel concerns a measure as it existed at the time the panel was established, a recommendation is prospective in nature in the sense that it has an effect on, or consequences for, a WTO Member's implementation obligations.").

[21] DSU, Art. 19.1 (emphasis added).

recommendation where it has found a measure within its terms of reference to be inconsistent with the relevant Member's obligations.

18. In contrast, footnote 33, paragraph 7.13, of the Panel's report expresses a view that, where challenged measures have expired and ceased to have legal effect, it is not "possible . . . for the Panel to issue *meaningful* recommendations under Article 19.1 of the DSU."[22] The Panel further suggests that even where a recommendation is possible, it may be "inutile" to do so in other scenarios.[23]

19. The United States sympathizes with the EU's frustration in the continuation of a dispute that appears to have been successfully resolved. That being the case, we would urge Pakistan to strongly consider whether it is necessary to continuing pressing this appeal. In the circumstance where a contested measure has expired and the complainant agrees it is no longer in effect, the parties should consider whether a mutually agreed solution may be reached pursuant to DSU Article 3.6. Indeed, the DSU encourages such solutions.[24] If Pakistan and the EU are able to reach a resolution, then there would be no need to spend the limited time and resources of the Secretariat and the Appellate Body Members to continue the appellate proceedings.

20. However, if the parties cannot arrive at a mutually satisfactory solution, then these proceedings should continue in a way that preserves the rights and obligations of both parties under the DSU.[25] The United States considers that denying Pakistan a recommendation with respect to the measure at issue would prejudice its rights under the DSU.

21. If panels and the Appellate Body, contrary to DSU Article 19.1, fail to make recommendations on WTO-inconsistent measures because they have expired or changed during the course of panel or appellate proceedings, a responding party could theoretically avoid compliance with its WTO obligations by withdrawing a contested measure during the proceedings, and then later re-imposing it. Without a recommendation under Article 19.1, the responding Member would have no prospective implementation obligation with respect to that WTO-inconsistent measure,[26] and the complaining Member would have no right to request review of the respondent Member's action under Article 21.5 of the DSU.[27] Such an outcome

[22] Panel Report, para. 7.13, n.33 (emphasis added).

[23] Panel Report, para. 7.13.

[24] *See, e.g.*, DSU, Art. 3.7 ("A solution mutually acceptable to the parties to a dispute and consistent with the covered agreements is clearly to be preferred.").

[25] *See* DSU, Art. 3.2 ("The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it serves to preserve the rights and obligations of Members under the covered agreements . . . .").

[26] *See, e.g., China – Raw Materials (AB)*, para. 260 ("While a finding by a panel concerns a measure as it existed at the time the panel was established, a recommendation is prospective in nature in the sense that it has an effect on, or consequences for, a WTO Member's implementation obligations.").

[27] *See* DSU, Art. 21.5 ("Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures.").

would necessarily diminish the rights of affected parties under the covered agreements, as well as the obligations of the offending party.[28]

22. The United States also observes that, in failing to make a recommendation based on the expiration of the offending measure, the Panel in this dispute appears effectively to have made a finding that the EU *has complied* with the recommendation that the Panel might otherwise have made, and extinguished Pakistan's rights under Article 21.5 on that basis. That is, despite its finding that there was "a reasonable possibility that the European Union could impose CVDs on Pakistani goods in a manner that may give rise to certain of the same, or materially similar, WTO inconsistencies that are alleged in this dispute," the Panel denied Pakistan the right to address any such re-imposition by failing to issue a recommendation regarding the WTO-inconsistent measure.[29] If the hazard of which the Panel warns were to occur, the Panel's findings alone could not remedy this denial. Without a recommendation, Pakistan could not pursue further claims under Article 21.5 of the DSU.

23. Of particular concern to the United States is the Panel's failure to examine in its analysis the text of Article 19.1 of the DSU. Instead, the Panel referred to prior reports that, in its view, suggest that the issuance of a recommendation is discretionary. Neither this panel, nor those reports, address the mandatory text of Article 19.1 directly. Therefore, there is no basis in the DSU for the Panel's approach.

24. For reasons discussed in the previous section, the United States agrees with Pakistan that the Panel did not err in making findings on the EU measure, because it was in force at the time of the establishment of the Panel and within the Panel's terms of reference. Having found an inconsistency, however, the United States considers that the Panel was obligated under Article 19.1 of the DSU also to issue a recommendation with respect to the WTO-inconsistent measure. Therefore, if the Appellate Body finds the EU measure to be inconsistent with the SCM Agreement, it must recommend that the EU bring its measure into compliance, as required under Article 19.1, unless the parties agree that not issuing a recommendation will assist them in securing a positive resolution to this dispute. We understand that Pakistan does not appeal the Panel's failure to issue a recommendation. Therefore, this unique circumstance appears to be present in this dispute.

## III. THE EUROPEAN UNION'S CLAIMS OF ERROR WITH REGARD TO THE PANEL'S ANALYSIS UNDER ARTICLE 1.1(a)(1)(ii), FOOTNOTE 1, AND ANNEXES I TO III OF THE SCM AGREEMENT

25. In this appeal, the EU argues that the Panel misinterpreted Article 1.1(a)(1)(ii) and footnote 1 of the SCM Agreement, read in light of Annexes I through III of that Agreement.[30] The United States agrees that the Panel's legal interpretation of the SCM Agreement was

[28] DSU, Art. 3.2 ("Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.").

[29] Panel Report, para. 7.13.

[30] EU Appellant Submission, paras. 68-83.

erroneous and the Appellate Body should reverse the Panel's findings under Article 1.1(a)(1)(ii).[31]

26. Below, the United States sets out what, in its view, is the proper framework for considering whether an investigating authority's treatment of a duty drawback system such as the MBS is consistent with the relevant provisions of the SCM Agreement. The Panel erred in its interpretation of Articles 1.1(a), footnote 1, the Illustrative List of Export Subsidies (Annex I), and the examination steps found in Annexes II and III.

### A. Panel Findings Regarding Article 1.1(a)(1)(ii) and Footnote 1

27. The Panel determined that "[t]he language 'shall not be deemed to be a subsidy' in footnote 1 indicates that, in the absence of further qualification, the two situations described [in the footnote] are never subsidies under Article 1."[32] With respect to the remission of duties specifically, the Panel further found that "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."[33] Denominating it the "Excess Remissions Principle," the Panel concluded that "[a] subsidy exists insofar as the former exceeds the latter, i.e. an 'excess' remission occurs representing revenue forgone otherwise due."[34]

28. In response to the EU's argument that the footnote only operates to preclude the finding of a subsidy based on a financial contribution in the form of revenue forgone if the requirements of Annexes II and III are satisfied, the Panel disagreed. In the Panel's view, the phrase "[i]n accordance with" indicates that the "Excess Remission Principle" enunciated in the footnote was, as stated, "in conformity with" Article XVI of GATT 1994 (Note to Article XVI) and Annexes I through III.[35] The Panel considered it "incongruous to say that a principle is in agreement with a provision when the provision potentially eliminates the principle," and noted that it found "no other instance in which the SCM Agreement uses the term 'in accordance with', on its own, to create an exception to an otherwise stated rule by cross-referencing another provision."[36] The Panel concluded that, even if a duty drawback scheme does not satisfy either of the two conditions in Annex II(II) of the SCM Agreement (i.e., where the exporting Member (1) "has no reliable system of tracking inputs" and (2) "in the absence of further examination by the exporting Member"), "investigating authorities should still determine if an excess remission occurred."[37]

29. Based on its interpretation of the relevant provisions of the SCM Agreement and GATT 1994, the Panel found that the EU Commission "offered no reasoned and adequate explanation

[31] Given the entirely consequential nature of the Panel's finding under Article 3.1(a) of the SCM Agreement, the United States does not specifically comment on this finding.

[32] Panel Report, para. 7.37.

[33] Panel Report, para. 7.37.

[34] Panel Report, para. 7.37.

[35] Panel Report, para. 7.39.

[36] Panel Report, para. 7.40.

[37] Panel Report, para. 7.56.

for why the entire amount of unpaid duties was a financial contribution and that those duties were 'in excess of those which have accrued' within the meaning of footnote 1 of the SCM Agreement, and thus acted inconsistently with Article 1.1(a)(1)(ii) of the SCM Agreement."[38]

### B. Article 1.1 and Footnote 1

30. Article 1.1(a)(1)(ii) of the SCM Agreement provides that "a subsidy shall be deemed to exist if: . . . . government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits)."

31. Footnote 1 to that provision explains:

> 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.

This exemption is rooted in the Ad Note to Article XVI of GATT 1994 and is based almost verbatim on that language.

32. Both footnote 1 to the SCM Agreement and the Ad Note to Article XVI of the GATT 1994 contemplate that a duty drawback scheme "shall not be deemed to be a subsidy" so long as there is no "excess" remission of duties or taxes from those which have accrued. Consequently, if a duty drawback system were to provide for exemption or remission of duties or taxes in amounts that exceed the amounts of "duties or taxes that have accrued," then such a system may be "deemed to be a subsidy" under the terms of Article 1.1 of that Agreement.

33. Importantly, footnote 1 also notes that this standard (that "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") is "[i]n 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." Article 32.8 of the SCM Agreement provides that "[t]he Annexes to this Agreement constitute an integral part thereof."

34. Annex I to the SCM Agreement, providing an "illustrative list" of export subsidies, elaborates that the "[t]he remission or drawback of import charges in excess of those levied on imported inputs that are consumed in the production of the exported product (making normal allowance for waste)" would constitute an "export subsidy."[39] Again, this suggests that an export subsidy exists in cases where there is such an excess.

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[38] Panel Report, paras. 7.58, 7.60. The Panel also found that, "[b]ecause the Commission . . . incorrectly identified the existence of a subsidy," the EU "acted inconsistently with Article 3.1(a) [of the SCM Agreement] by improperly finding the existence of a 'subsidy' that was contingent on export performance." *Id.* at para. 7.60.

[39] Article 3.1(a) explains that subsidies that are contingent upon export performance, "including those illustrated in Annex I," are "prohibited," although those referenced in Annex I as not constituting export subsidies are not prohibited. Annexes II and III also clarify that duty drawback systems can constitute export subsidies to the extent

35. In determining whether a duty drawback scheme provides for remission of import duties in amounts that in fact exceed a permitted limit, the procedures described in Annexes II and III are pertinent. The standard in footnote 1 to the SCM Agreement is "in accordance with" Annexes II and III, which each addresses a particular duty drawback scheme. Annex I, item (i), also states that "[t]his item shall be interpreted in accordance with the guidelines on consumption of inputs in the production process contained in Annex II and the guidelines in the determination of substitution drawback systems as export subsidies contained in Annex III."

36. Annexes II and III provide for steps to check that the system of the exporting Member operates so as not to provide for excess remission of import duties.[40] Annex II(II)(1) provides that the investigating authority should first determine whether the exporting Member has in place an adequate system or procedure to monitor which inputs are consumed in the production of the exported product and in what amounts. Again, Annex I, item (i) states that the amount of "excess" is a direct function of how much of the imported input is "consumed in the production of the exported product." Thus, Annex II(II)(1) explains that:

> Where it is alleged that an indirect tax rebate scheme, or a drawback scheme, conveys a subsidy by reason of over-rebate or excess drawback of indirect taxes or import charges on inputs consumed in the production of the exported product, the investigating authorities should first determine whether the government of the exporting Member has in place and applies a system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts. Where such a system or procedure is determined to be applied, the investigating authorities should then examine the system or procedure to see whether it is reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export. The investigating authorities may deem it necessary to carry out, in accordance with paragraph 6 of Article 12, certain practical tests in order to verify information or to satisfy themselves that the system or procedure is being effectively applied.

37. Annex II(II)(2) contemplates an additional analysis by the exporting Member absent satisfaction of the condition under Annex II(II)(1). That paragraph states that:

> Where there is no such system or procedure, where it is not reasonable, or where it is instituted and considered reasonable but is found not to be applied or not to

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they allow for excess remission or drawback of import charges. *See* Annex II(I)(2) ("Pursuant to paragraph (i) [of Annex I], drawback schemes can constitute an export subsidy to the extent that they result in a remission or drawback of import charges in excess of those actually levied on inputs that are consumed in the production of the exported product . . . normal allowance for waste must be made in findings regarding consumption of inputs in the production of the exported product"); Annex III(I) to the SCM Agreement ("substitution drawback systems can constitute an export subsidy to the extent that they result in an excess drawback of the import charges levied initially on the imported inputs for which drawback is being claimed").

[40] Although Annex III is not squarely applicable to this dispute, Annex III(II)(1) identifies the importance of this precision: "[t]he existence of a verification system or procedure is important because it enables the government of the exporting Member to ensure and demonstrate that the quantity of imports for which drawback is claimed does not exceed the quantity of similar products exported, in whatever form, and that there is not drawback of import charges in excess of those originally levied on the imported inputs in question").

> be applied effectively, a further examination by the exporting Member based on the actual inputs involved would need to be carried out in the context of determining whether an excess payment occurred. If the investigating authorities deemed it necessary, a further examination would be carried out in accordance with paragraph 1.

38. Where an exporting Member has a duty drawback scheme in place that does not satisfy the requirements for such a scheme to "not be deemed to be a subsidy"[41] pursuant to Annex II(II)(1)-(2), then an investigating authority would be permitted to consider the full amount of the remission as a financial contribution under the terms of Article 1.1(a). This is because, as the United States discusses in further detail below, the conditions for a duty drawback scheme to be considered within the scope of footnote 1 to Article 1.1(a)(1)(ii) of the SCM Agreement as not providing for "excess" remission are established by reference to Annex II(II)(1)-(2).

39. If, on the other hand, following the steps in Annexes II and III, the investigating authority is able to confirm that the remitted amounts are not in excess of those accrued, the drawback system falls into the category of permissible drawback systems eligible for the exemption under footnote 1.

### C. The Panel's Analysis of the Commission's Determination Is in Error

40. We do not consider that the Panel's "Excess Remissions Principle" appropriately describes the function of footnote 1 because it ignores the broader context and requirements contained in Annexes I through III. In finding that an investigating authority may never treat the full amount of import duties remitted under a duty drawback scheme as a financial contribution, even where the drawback scheme does not satisfy the conditions in Annex II(II) to the SCM Agreement, the Panel misread the "in accordance with" language in footnote 1.[42] Although the Panel explained that "the Excess Remissions Principle is 'in agreement with', 'in conformity with' and/or 'in harmony with'" Ad Note to Article XVI and Annexes I through III of the SCM Agreement, the Panel incorrectly concluded that "[t]he footnote refers to these provisions equally, suggesting that the Excess Remissions Principle is equally in agreement with each."[43] In other words, the Panel adopted this principle as a uniform rule that applies throughout the SCM Agreement and looked at whether there are permissible departures from,[44] limitations of, or exceptions to[45] that principle.[46] Respectfully, the Panel scrutinized the wrong issue. The issue is not whether there are exceptions to footnote 1. The relevant issue is how footnote 1 should be interpreted in a particular proceeding, based on the nature of the duty drawback scheme at issue before the investigating authority in that proceeding. This is where the other provisions cited in footnote 1 become pertinent.

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[41] Footnote 1 to Article 1.1(a)(1)(ii) of the SCM Agreement.

[42] *See* Panel Report, para. 7.56.

[43] Panel Report, para. 7.39. The United States agrees with the EU's criticism of this interpretation. *See* EU Appellant Submission, para. 69.

[44] Panel Report, para. 7.56.

[45] Panel Report, para. 7.40.

[46] *See* Pakistan Appellee Submission, para. 2.54.

41. Contrary to the Panel's conclusion, the phrase "in accordance with" signals that it is footnote 1 that is to be interpreted "in harmony with" Article XVI of the GATT 1994 (Note to Article XVI) and Annexes I-III of the SCM Agreement.[47] In reading this language as a hortatory confirmation of consistency with other provisions, the Panel's interpretation essentially reads footnote 1 backwards, reading out of the footnote the references to Annexes I through III altogether, and rendering inoperative the extensive requirements set out in those Annexes as they relate to duty drawback and other remission schemes. This is also inconsistent with Article 32.8 of the SCM Agreement, which clarifies that "[t]he Annexes to this Agreement constitute an integral part thereof."

42. Annex I, item (i) to the SCM Agreement clarifies that an export subsidy exists where there is excess "remission or drawback of import charges." Although the Panel notes the first sentence of Annex I, item (i) restates the so-called "Excess Remissions Principle," the Panel failed to meaningfully engage with the second sentence of that provision.[48] The second sentence explains that "[t]his item shall be interpreted in accordance with the guidelines on consumption of inputs in the production process contained in Annex II and the guidelines in the determination of substitution drawback systems as export subsidies contained in Annex III."[49] In other words, the "Excess Remissions Principle" stated in Annex I, item (i) – like footnote 1 – "shall be interpreted" "in harmony with"[50] the guidance contained in Annexes II and III.[51]

43. Annex II(I)(2) restates Annex I, item (i). Thus, drawback schemes can constitute export subsidies to the extent they result in remission of import duties in excess of those actually levied on inputs consumed in the production of the exported product.[52] But in considering paragraph II, the Panel rendered that part of Annex II inutile. Such a reading is in error.

44. Annex II(II) provides "guidance for investigating authorities" regarding "how to determine 'whether inputs are consumed in the production of the exported product'."[53]

45. Annex II(II) is key to interpreting footnote 1; Annex I, item (i); and Annex II(I). This is because a determination of what inputs are consumed directly informs the analysis of whether there is any excess remission of import duties in connection with those inputs. Even the Panel observed – correctly – that the question of "how to determine 'whether inputs are consumed in the production of the exported product' . . . *is an intermediate, but necessary, factual issue* to address when determining whether excess payments occurred under a drawback scheme."[54] In other words, Annex II(II) informs whether a purported duty drawback scheme falls within the scope of footnote 1 such that it "shall not be deemed to be a subsidy" or whether it conveys a

[47] *See* EU Appellant Submission, para. 71 ("the situation described in the second part of the sentence in footnote 1 is qualified by the first part of the same sentence by the terms 'in accordance with', thereby making reference to the elements that must be taken into account to determine whether said situation benefits from the carve-out").

[48] Panel Report, para. 7.44, n.102.

[49] Item (i) of Annex I to the SCM Agreement (emphasis added).

[50] Panel Report, para. 7.39.

[51] *See* item (i) of Annex I to the SCM Agreement; *see also* EU Appellant Submission, para. 72.

[52] Panel Report, para. 7.47.

[53] Panel Report, para. 7.49.

[54] Panel Report, para. 7.49 (emphasis added).

financial contribution and to what extent, such that the measure is appropriately considered a subsidy otherwise falling under Article 1.1.

46. The focus of the procedures under Annex II(II)(1)-(2) is to identify whether excess remission of duties under a duty drawback scheme is occurring, based on the actual imported inputs that are subject to drawback that are used in the production of the exported product. Those procedures contemplate that it is possible for an exporting Member to demonstrate, for example under Annex II(II)(2), that there is no excess remission under its duty drawback scheme. As an alternative, it is possible that an exporting Member can demonstrate that it tracks the imported inputs that are subject to drawback and show that there is a precise amount of excess remission. Of course, because that excess remission would be "deemed to be a subsidy" under footnote 1, an investigating authority may treat it as a financial contribution consistent with Article 1.1(a). However, Annex II(II)(1) and (2) both contemplate that the exporting Member, as part of its duty drawback scheme, must be able to track the inputs consumed in the production of the ultimately exported product that are subject to such drawback. If the exporting Member cannot demonstrate that it can track the inputs used in the production of the exported product under investigation, then an investigating authority is permitted to conclude that the drawback scheme does not satisfy the analytical criteria in Annex II. In that situation, it may be appropriate for the investigating authority to treat the full amount of duties otherwise due to the exporting Member as a financial contribution – and thus a subsidy – under Article 1.1(a).

47. With regard to this latter situation, of particular concern to the Panel appears to be its understanding that Annex II(II)(2) "does not indicate what happens if the 'further examination' that 'would need to be carried out' is not performed" by the exporting Member.[55] As the Panel properly observed, "Annex II provides incomplete guidance as to how to investigate a particular issue in this context."[56] Yet in response to this incomplete guidance, the Panel's interpretation simply shifts the responsibility for determining consistency with Annex II(II) from the exporting Member to the investigating authority. By requiring investigating authorities to determine some (less than full) amount of excess remission, even where the exporting Member cannot make the demonstration under Annex II(II),[57] the Panel's interpretation "would require investigating authorities to essentially administer another Member's duty drawback system in the event that the system is found to be deficient under Annex II(II)."[58] This is not supported by the text of Annex II(II).

48. To the contrary, Annex II(II)(1)-(2) contemplates a system that in itself can demonstrate that there is no excess remission on the part of the exporting Member. In that respect, the United States agrees with the EU that "[l]imiting classification as a 'subsidy' solely to the excess remitted or refunded" in all circumstances "*presupposes* that the system for remission or exemption of import duties is compatible with the Annexes I to III, since in those cases exporters

[55] Panel Report, paras. 7.50, 7.52; *see also* EU Appellant Submission, para. 74.

[56] Panel Report, para. 7.51.

[57] Panel Report, para. 7.56.

[58] Panel Report, para. 7.59.

are indeed 'entitled' to drawback in respect of duties on the inputs used in the exported products."[59]

49. As discussed above, the conditions for a duty drawback scheme to be considered within the scope of footnote 1 are established by reference to Annex II(II)(1)-(2). Therefore, an exporting Member's ability to track the inputs used in the production of an exported product is a central feature of a duty drawback scheme for purposes of the SCM Agreement. If an exporting Member cannot make the demonstration that its measure satisfies those conditions, then an investigating authority would have no way of knowing that the measure is actually in the form of a duty drawback scheme subject to (i.e., "in accordance with") footnote 1 in the first place.[60] The conditions in Annex II(II) thus serve to limit the exclusion in footnote 1 by preventing exporting Members from shielding their exporting producers from the disciplines of Article 1.1(a)(1)(ii) of the SCM Agreement simply by labeling a measure as a "duty drawback scheme."[61] For this reason, where a purported remission of duties does not satisfy the requirements found in the Annexes, an investigating authority is permitted to examine that measure as a financial contribution under Article 1.1 as it would any other measure, and, if appropriate, to countervail the full amount of the financial contribution.

## IV. CONCLUSION

50. For the foregoing reasons, the United States considers that (1) the Panel did not err in deciding to make findings with respect to an expired measure; and that (2) the Panel erred in its interpretation and application of Article 1.1(a), footnote 1, Article 3.1(a), the Illustrative List of Export Subsidies (Annex I), and the provisions of Annexes II and III. If the Appellate Body finds that the CVD measure at issue is inconsistent with the EU's obligations under the SCM Agreement, the United States also considers that, pursuant to Article 19.1 of the DSU, the Appellate Body must recommend that the EU bring its measure into compliance with those obligations unless the Parties agree that not issuing a recommendation will assist them in securing a positive resolution to this dispute.

51. The United States appreciates the opportunity to provide its views in this appeal and hopes that its comments will be useful to the Appellate Body.

[59] EU Appellant Submission, para. 79 (emphasis in original).

[60] *See* EU Appellant Submission, paras. 59, 69.

[61] *See* EU Appellant Submission, para. 78.