EUROPEAN UNION – COUNTERVAILING MEASURES ON CERTAIN POLYETHYLENE TEREPHTHALATE FROM PAKISTAN (DS486)

THIRD PARTY EXECUTIVE SUMMARY OF THE UNITED STATES OF AMERICA

October 7, 2016

EXECUTIVE SUMMARY OF U.S. THIRD PARTY WRITTEN SUBMISSION

I. INTRODUCTION

1. In this submission, the United States presents its views on the proper legal interpretation of certain provisions of the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement") and the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994") as relevant to certain issues in this dispute.

II. CLAIMS REGARDING ARTICLES 1 AND 3 OF THE SCM AGREEMENT

2. The United States, while taking no position on the merits of the factual allegations made by either party, submits the following comments. The core disagreement between the parties is whether it is legally permissible under the SCM Agreement to treat the entire amount of import duties otherwise due on imported inputs under a duty drawback system as a financial contribution under Article 1.1 where the exporting Member: (1) does not have an effective system or procedure in place to monitor the inputs consumed in the production of the exported product and (2) has failed to carry out a further examination based on the actual inputs involved in determining whether an excess payment occurred under the duty drawback scheme. The United States submits that this question should be answered in the affirmative under the relevant provisions of the SCM Agreement and the GATT 1994.

3. 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.

4. 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."

5. 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." Again, this suggests that an export subsidy exists in cases where there is such an excess.

6. 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."

7. For a duty drawback system to operate so as not to provide for excess remission of import duties, Annexes II and III provide for procedures to check the system of the exporting Member. 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. Annex II(II)(2) contemplates an additional analysis by the exporting Member absent satisfaction of the condition under Annex II(II)(1).

8. Therefore, 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," then an investigating authority would be permitted to consider the full amount of the financial contribution as a subsidy under the terms of Article 1.1. 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 are established by reference to Annex II(II)(1)-(2).

9. Finally, an investigating authority need not consider information that post-dates the period of investigation in trade remedy proceedings.

III. CLAIMS REGARDING ARTICLES 1.1(B) AND 14 OF THE SCM AGREEMENT

10. Because the title of Article 14 indicates that it sets out "guidelines" for determining benefit, there exists "a certain degree of flexibility … under Article 14(b) in the selection of benchmarks." The selection of an appropriate benchmark under Article 14(b) is guided by the terms "comparable," "commercial," and a "loan which the firm could actually obtain on the market."

11. Of particular relevance to this dispute, the comparable commercial loan benchmark must be contemporaneous in time with the alleged subsidized loan. For example, in *EC and certain member States – Large Civil Aircraft*, the Appellate Body explained that investigating authorities must rely on a benchmark "that would have been available to the recipient firm at the time it received the government loan," such that the comparison to determine the benefit "is to be performed as though the loans were obtained at the same time." This contemporaneity factor accords with the principle that "[t]he investor will make its decision to invest on the basis of information available at the time the decision is made about market conditions and projections about how those economic conditions are likely to develop (future demand and price for the product, future costs, etc.)."

12. Finally, Article 14(b) also describes a benchmark loan as reflecting one "which the firm could actually obtain on the market." The Appellate Body has explained that "[t]he use of the conditional tense, 'could', suggests that a benchmark loan under Article 14(b) need not in every case be a loan that exists or that can *in fact* be obtained in the market." The Appellate Body has also observed that "could" refers "'first and foremost' to the borrower's risk profile, that is,

whether the benchmark loan is one that could be obtained by the borrower receiving the investigated government loan." Given these findings, the United States agrees with Pakistan's observation that "the investigating authority must, at the very least as the starting point of its analysis, first seek to identify a comparable loan that *the specific firm* under investigation would pay."

13. In light of the guideline of comparing the transaction to one the loan recipient might have obtained on the market, an investigating authority might well examine the transaction and rely on a benchmark that is contemporaneous with when the loan disbursement terms were established. This is because the investigating authority could take the view that each tranche is merely a part of the one overall loan. The investigating authority might also examine the transaction and apply a loan interest rate benchmark that is contemporaneous in time with when each tranche of the investigated loan was drawn down, as Pakistan proposes, because the authority might determine that each tranche should be considered as a distinct loan. These considerations will depend on the factual circumstances concerning the terms of the loan.

14. Finally, the United States observes that an investigating authority has an obligation to provide a transparent and adequate explanation for why it selected a particular benchmark. One reason is so the parties to the investigation can adequately and timely defend their interests.

IV. CLAIMS REGARDING ARTICLE 12.6 OF THE SCM AGREEMENT

15. The last sentence of Article 6.7 of the AD Agreement largely mirrors the last sentence of Article 12.6 of the SCM Agreement. The last sentence of Article 6.7 of the AD Agreement requires investigating authorities "to inform the investigated exporters of the verification results," *i.e.*, the results of the verification visit. The disclosure of the results of a verification visit are important both in enabling exporters and WTO Members to seek judicial review of the investigating authority's determination under Article 23 of the SCM Agreement, and to protect exporters' rights to prepare and present their cases under Article 12.3 of the SCM Agreement.

16. The meaning of the term "results" in the last sentence of Article 12.6 of the SCM Agreement informs the extent of what the investigating authority must provide to "the firms to which they pertain." The ordinary meaning of "result" is "an effect, issue, or outcome *from* some action, process or design." The "results" envisaged by Article 12.6 of the SCM Agreement are the "outcome" of the verification visit, which under Annex VI(7) is an on-the-spot investigation "to verify information provided or to obtain further details."

17. Article 12.6 of the SCM Agreement (as does Article 6.7 of the AD Agreement) provides two alternative mechanisms for disclosing the verification visit results: to make the results available to the firm to which the results pertain or to disclose the results as part of the essential facts which form the basis for a decision to impose definitive measures. Thus, one such option is to "'make available' a separate report containing the results of the verification visits."

18. Consequently, the Panel should consider whether Pakistan has demonstrated that the Commission's disclosure of the verification visit results was not sufficient to disclose the

outcome of the verification, was not complete such that essential facts were not disclosed, or was not timely such that interested parties were not able to defend their interests.

EXECUTIVE SUMMARY OF U.S. THIRD-PARTY ORAL STATEMENT AT THE THIRD PARTY SESSION OF THE FIRST MEETING OF THE PANEL WITH THE PARTIES

V. INTRODUCTION

19. The United States appreciates the opportunity to provide our views as a third party in this dispute. The United States will focus its remarks on the interpretation and application of Article 1 of the SCM Agreement, particularly in light of issues raised by Pakistan with respect to footnote 1 of Article 1.1 and the operation of the annexes related to these provisions.

VI. ARTICLE 1.1 AND FOOTNOTE 1 OF THE SCM AGREEMENT

20. Article 1.1(a)(1)(ii) is accompanied by footnote 1. Footnote 1 does two things: first, it limits the scope of Article 1.1 subparagraph (a)(1)(ii) where the remission of certain duties or taxes is not in excess of accrued amounts; and second, it requires that this limitation be read "in accordance with" Annexes I, II, and III in determining its applicability. Consequently, if a program were to provide for the exemption or remission of duties or taxes in amounts that exceed the "duties or taxes that have accrued" in a given instance, then such excess may be "deemed to be a subsidy" under the text of Article 1.1 of the SCM Agreement. To reach such a conclusion in the first place, however, the question of excess remission must be answered per the guidelines and procedures of the relevant annexes. Where that inquiry is inconclusive, the limitation found in footnote 1 does not apply and, therefore, an investigating authority may determine whether there is a financial contribution irrespective of footnote 1.

21. This interpretation is supported by the language of the annexes themselves. The procedures described in Annex II, in particular, are pertinent in determining whether there is remission of import duties in amounts that in fact exceed a permitted limit. Annex II(II) provides for a two-step analysis for investigating authorities to confirm whether the scheme in question provides for excess remission of import duties.

22. Should the system not satisfy the conditions in Annex II(II)(1), Annex II(II)(2) contemplates an additional analysis by the exporting Member. Specifically, subparagraph (II)(2) provides that the exporting Member take steps to demonstrate the validity of its system in three different scenarios. In each of those scenarios, the step of demonstrating that there is no excess remission is left to the exporting Member. Specifically, the exporting Member would need to carry out a "further examination . . . based on the actual inputs involved" to determine "whether an excess payment occurred." Otherwise, the investigating authority would have to determine amounts where not possible per the annex guidelines. Such a result would not be consistent with meaning of these provisions.

23. It is for this very reason that both subparagraphs (1) and (2) to Annex II(II) require that the exporting Member ensure and demonstrate that there is no excess remission of import duties.

If the exporting Member cannot demonstrate that it has an adequate system or procedure in place or that there are otherwise no excess import duties remitted, then it would be impossible for the investigating authority to make such a determination.

24. An investigating authority must be able to identify with some precision the extent to which there is excess duty remission under the system in order to determine whether the limitation provided for in footnote 1 applies to the particular financial contribution at issue. Neither the footnote, nor the referenced annexes, suggests their purpose relates to the determination of subsidy amounts. This is particularly true where the investigating authority cannot discern whether, and to what extent, there is excess remission, because the exporting Member has not been able to make the required demonstration.

25. Thus, the language of the annex supports the interpretation of the United States that footnote 1 operates to limit the definition of a financial contribution set forth in Article 1.1(a)(1)(ii). Where the criteria for this limitation are not satisfied per the guidelines of Annex II, the limitation does not apply, and the language of footnote 1 has no further bearing on the question of whether the alleged program is a financial contribution.

VII. CHANGES AFTER THE PERIOD OF INVESTIGATION

26. Finally, the United States notes that an investigating authority need not consider information that post-dates the period of investigation in a trade remedy proceeding. Rather, the authority must consider the system or procedure that was in place during the period of investigation.

EXECUTIVE SUMMARY OF U.S. RESPONSES TO PANEL QUESTIONS TO THIRD PARTIES

27. In the context of an investigation, if the investigating authority cannot satisfy itself that the exporting Member has an adequate verification system or procedure in place under Annex II(II)(1), or the exporting Member does not demonstrate that there are otherwise no excess import duties remitted pursuant to Annex II(II)(2), then there is no textual basis for the investigating authority to make a determination *per footnote 1* that the alleged financial contribution shall "not be deemed to be a subsidy." Thus, where the inquiry posed by Annex II(II) is inconclusive, the limitation in footnote 1 to Article 1.1(a)(1)(ii) does not apply and an investigating authority may determine whether there exists a financial contribution irrespective of footnote 1.

28. Assuming an exporting Member has no "system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts," the only remaining step through which an exporting Member may comport with Annex II (and, therefore, footnote 1) is for the exporting Member to perform the "further examination" as envisioned by Annex II(II)(2). The exporting Member's opportunity to perform that examination is not contingent upon a request for such action on the part of an investigating authority.

29. In the view of the United States, the analysis under subparagraphs (II)(1) and (2) is sequential. Thus, absent satisfaction of the criteria in paragraph 1, a "further examination by the exporting Member… would need to be carried out". Nothing in the text of paragraph 2 suggests that the investigating authority must request that the exporting Member carry out the "further examination" "[w]here there is no such system or procedure" (as is assumed by the Panel's question).

30. Suppose that, prior to verification, an exporting Member has acknowledged in its questionnaire response that its duty drawback scheme lacks a verification system or procedure under Annex II(II)(1), but has also submitted evidence of the results obtained from conducting a further examination of the amount of excess remission based on actual inputs consumed, pursuant to Annex II(II)(2). In this scenario, the investigating authority could take that information into account in determining whether a subsidy exists and the extent of the benefit. During on-the-spot verification, the investigating authority would then be able to "satisfy itself" as to the veracity of the evidence already submitted.

31. By contrast, suppose that an exporting Member has asserted, prior to verification, that its duty drawback scheme comports with Annex II(II)(1), but has not undertaken "a further examination" as described by Annex II(II)(2). An investigating authority then conducting a verification to "satisfy itself" as to the veracity of the evidence already submitted would be able to spot-check the basis for the Annex II(II)(1) assertion, but would have nothing to "verify" regarding Annex II(II)(2) if no "further examination" had been conducted by the exporting Member.

32. Whether the entire amount of duty remission or an "excess" amount is countervailed would depend on the factual circumstances confronted by an investigating authority.

33. In response to the Panel's final question, generally speaking, a "line of credit" can be considered a type of loan. In considering whether a loan benchmark is "comparable," the investigating authority should consider a benchmark that "'ha[s] as many elements as possible in common with the investigated loan . . .'," although "in practice, the existence of such an ideal benchmark loan would be extremely rare," and "a comparison should also be possible with other loans that present a lesser degree of similarity." As we have noted, this suggests that factual circumstances are central to the benchmark selection.