

## The Age of Innocence

Rubini, Luca

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## Research at Birmingham

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## **The age of innocence - The evolution of the case-law of the WTO dispute settlement: Subsidies as a case-study.**

**Luca Rubini<sup>1</sup>**

### *Abstract*

Through the analysis of the topical and salient jurisprudence on subsidies and countervailing duties, this paper attempts to trace the development of the role of dispute settlement in the WTO in its first twenty years. Against a paradigmatically unclear regulatory framework, what has been the attitude of the Panels and the Appellate Body during this long period? Was the first phase of dispute settlement one of simple discovery? Has this progressively made way for a more active approach towards the law, which could be – and has been - tagged ‘activism’? Using representative examples of subsidy decisions by Panels and the Appellate Body, this paper argues that the Panels are on the whole more self-restrained than the Appellate Body. Furthermore, the latter is increasingly departing from its original ‘textual’ approach and adopting innovative decisions, which either raise serious doubts about their correctness or should be assessed as being plainly wrong. The paper advocates that WTO adjudicating bodies should pay more attention to the ‘negotiated balance’ and the ‘point of balance’ of the various disciplines in the SCM Agreement and that, in this respect, a stronger use of the negotiating history is necessary.

Key words: WTO – subsidies – SCM Agreement – jurisprudence – Appellate Body – legal interpretation

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<sup>1</sup> Reader in International Economic Law, University of Birmingham Law School, contact: [lrubini@bham.ac.uk](mailto:lrubini@bham.ac.uk). I am grateful for the useful comments and suggestions received by Lorand Bartels, Tomer Broude, Ben Cznarnik, Claus-Dieter Ehlermann, Gary Horlick, Simon Lester, Petros Mavroidis, Joost Pauwelyn, Mona Pinchis and Julia Qin on previous versions of this paper. Special thanks go to Isabelle Van Damme. Any mistake remains mine. This paper will be published also in Manfred Elsig, Bernard Hoekman and Joost Pauwelyn, *The WTO @ 20. World Trade Forum 2015* (Cambridge: Cambridge University Press, 2016).

## 1. The goal of the paper

The case law on subsidies and countervailing duties is topical and salient. The Agreement on Subsidies and Countervailing Measures (hereinafter ‘SCM Agreement’) is the third most litigated legal instrument in the World Trade Organization (WTO), after the General Agreement on Tariffs and Trade 1994 (‘GATT 1994’) and the Understanding on Rules and Procedures Governing the Settlement of Disputes (‘DSU’).<sup>2</sup> This significant and recurring litigation happens for essentially three main reasons. First, subsidies are a very important and common policy tool of governments, involving often high political stakes. Secondly, several measures can produce subsidy-like effects (i.e. creating economic and competitive advantages, tipping the ‘playing field’, creating possible obstacles to trade) with the result that the contours of what we mean by ‘subsidies’ are blurred. Thirdly, as a key instrument of government economic policy, subsidies are often motivated by legitimate public policy goals, which, in a global context, need to be traded off against the possible negative spillovers onto others. Hence – not only do we often not know what a subsidy is but also what constitutes a good or bad subsidy.

This multifactorial complexity explains why, during the Uruguay Round negotiations (and indeed the Tokyo Round), very different views on the regulation of subsidies clashed. The conclusion of an agreement was thus both a challenge and a success.<sup>3</sup> But a hefty price had to be paid. Subsidy rules lack clarity - paradigmatically.<sup>4</sup> This vagueness is a true test for those called to interpret the rules and make them operative. Consequently, subsidy jurisprudence represents a useful case-study of the WTO adjudicating bodies’ attitude to legal interpretation. It is only when dealing with hard cases and difficult interpretative questions that a court’s action is seriously verified.

WTO jurisprudence, and especially the decisions of the Appellate Body, are increasingly subject to criticism. Of particular interest is perhaps the disapproval expressed by people that have participated in negotiating the rules or held key positions in the GATT/WTO.<sup>5</sup> Given the prominent part subsidy laws play, it comes as no surprise that decisions on subsidies and countervailing duties are often in the

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<sup>2</sup> Focusing on appeals only, in the 1996-2014 period, after the DSU (100) and the GATT (85), there were 35 appeals implicating the SCM Agreement. See Appellate Body, *Annual Report for 2014*, WT/AB/24, 3 July 2015, p. 15.

<sup>3</sup> A recent account can be found in Luca Rubini, *What Shapes the Law? Reflections on the History, Law, Politics and Economics of International and European Subsidy Disciplines*, Global Governance Programme, European University Institute, 2016.

<sup>4</sup> The first example that is usually given to justify this statement is the lack of preamble to the SCM Agreement which reflects the huge divergences in positions of the negotiators.

<sup>5</sup> See, e.g., Frieder Roessler, ‘Changes in the Jurisprudence of the WTO Appellate Body during the Past Twenty Years’, Robert Schuman Centre for Advanced Studies, Global Governance Programme, Working Paper 2015/72; John D Greenwald, ‘A Comparison of WTO and CIT/CAFC Jurisprudence in Review of US Commerce Department Decisions in Antidumping and Countervailing Duty Proceedings’ (2013) *Tulane Journal of International and Comparative Law* 261-272; Michael Cartland, Gerard Depayre and Jan Woznowski, ‘Is Something Going Wrong in the WTO Dispute Settlement?’ (2012) *Journal of World Trade* 979-1016. See also Terence P Stewart, Patrick J McDonough, Jennifer M Smith and Sandra K Jorgensen, ‘The Increasing Recognition of Problems with WTO Appellate Body Decision-Making: Will the Message Be Heard?’ (2013) *Global Trade and Customs Journal* 390-412.

dock. Crucially, the criticism is not necessarily that the WTO dispute settlement organs sometimes take disputable or even wrong decisions, although this may happen and for various reasons. The gist of these criticisms is that certain decisions are wrong because they overlook the nature of WTO law, the ‘negotiated balance’ underlying it, and the corresponding role of WTO dispute settlement. This is particularly so for Appellate Body (also ‘AB’) reports (and less so for panel ones). This paper explores this line of criticism further, using the jurisprudence of subsidy laws as a testing ground. In so doing, the very interesting statements by current or former members of the Appellate Body, writing or speaking extra-judicially, are also considered, since they often assist in understanding the hermeneutic approach of the world trade court.<sup>6</sup>

The paper is structured as follows. After briefly outlining in Section 2 the jurisdiction and the rules of interpretation of panels and the Appellate Body, and introducing the concept of ‘negotiated balance’ in Section 3, in Section 4 I sketch few hypotheses with respect to the interpretative methods of Panels and Appellate Body in subsidy cases. Sections 5 and 6 set out to analyze two samples of cases where the dispute settlement bodies have arguably taken good and bad decisions respectively. Section 7 makes an initial assessment. Then Section 8 specifically examines the examples of good and bad decisions and investigates whether the search for the said ‘negotiated balance’ (could have) played any role in the interpretative process. Section 9 concludes.

## 2. The nature of WTO law and its dispute settlement

Space constraints permit only few remarks about the nature of WTO law and of its dispute settlement system.<sup>7</sup> In a nutshell, and at the risk of oversimplifying, my view is that, at least at its current stage of development, WTO law is more comparable to a contract (between parties) than to a constitution (of a community). Through this perhaps stark distinction, I define the fundamental premise of my argument, which is directly connected to the different attitudes the interpreter should have towards contractual vis-à-vis constitutional norms.<sup>8</sup> The interpretation of provisions of

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<sup>6</sup> See, e.g., Claus-Dieter Ehlermann, ‘Six Years on the Bench of the “World Trade Court” – Some Personal Experiences as Member of the Appellate Body of the World Trade Organization’ (2002) *Journal of World Trade*, 606; Georges Abi-Saab, ‘The Appellate Body and Treaty Interpretation’ in Giorgio Sacerdoti, Alan Yanovich and Jan Bohanes (eds.), *The WTO at Ten: The Contribution of the Dispute Settlement System* (Cambridge: Cambridge University Press, 2006); James Bacchus, ‘Appellators: The Quest for the Meaning of *and/or*’ (2005) *World Trade Review* 499-523; Jennifer Hillman, ‘An Emerging International Rule of Law? – The WTO Dispute Settlement System’s Role in its Evolution’ (2010-11) *Ottawa Law Review*, 269-284; Thomas Graham, ‘Present at the Creation’, speech at Hofstra University Law School, February 6, 2013. See also Joost Pauwelyn’s post ‘The Balancing Act of Keeping Up “Respect” for AB Rulings (according to an AB Member)’ in *International Economic Law and Policy Blog*, 15 February 2013.

<sup>7</sup> It is a topic that has generated an abundance of, often very differing, opinions. See, for example, John H. Jackson, *Sovereignty, the WTO, and the Changing Fundamentals of International Law* (Cambridge: Cambridge University Press, 2006); Robert Hudec, *Essays on the Nature of International Trade Law* (London: Cameron May, 1999); Joseph Weiler, *The EU, the WTO, and the NAFTA – Towards a Common Law of International Trade* (Oxford: Oxford University Press, 2000); Joost Pauwelyn, *Conflict of Norms in Public International Law. How WTO Law Relates to Other Rules of International Law* (Cambridge: Cambridge University Press, 2003).

<sup>8</sup> I will immediately explain what I mean by these two terms. The ‘contract’ vs ‘constitution’ distinction should not be confused with that between ‘rules’ and ‘standards’. See Louis Kaplow, ‘Rules Versus Standards: An Economic Analysis’ (1992–93) *Duke Law Journal* 557, 557

contractual nature normally involves placing special emphasis on the objective meaning coming out of their terms, these being the direct expression of the negotiations of the contracting parties and hence of their historical intent.<sup>9</sup> By contrast, (pace originalism's claims) constitutional provisions, especially those pertaining to general principles or fundamental rights, reflect a living document that relies less on historical intent and more on the present and future expectations of the community – while adhering perhaps to basic principles that are embedded in the document and depend on the special circumstances of its genesis. For these reasons, constitutions more easily lend themselves to creative and evolutive interpretation or require the continuous balancing of different interests and values.<sup>10</sup>

This premise involves that, at their current stage of evolution, WTO dispute settlement organs, and above all the Appellate Body, cannot be compared to domestic constitutional courts, or to international courts, like the Court of Justice of the European Union, that de facto have, or indeed have acquired, a constitutional status.<sup>11</sup> WTO panels and the Appellate Body cannot fill *significant* gaps or perform balancing acts of constitutional relevance.<sup>12</sup> They are akin to agents that have to respect the precise mandate given to them by their principals. If it is true that interpretation is always an act of construction of meaning,<sup>13</sup> in the WTO context it is also particularly true that there are rather defined limits to what the interpreter can and should do, especially when the rules are the result of a careful balancing between different positions. Against a world made up of compromises and creative ambiguity, and, crucially, in the absence of a clear mandate to ‘complete the contract’,<sup>14</sup> I am of the

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<sup>9</sup> This intent does not necessarily refer to agreeing a norm of clear and precise content, be it a principle or a right/obligation. The parties may simply agree on an ambiguous language, which is the expression of an ‘agreement to disagree’. As I note in Section 3 of this paper, the interpreter will thus have to do her or his best to identify this and proceed accordingly, for example by identifying any general common ground or, at the very least, what was certainly not contemplated by the parties.

<sup>10</sup> As noted, I am aware of the severity of the dichotomy I have introduced and of the possible freezing effect on the development of WTO law that this may imply. But the main issue, in my view, is that, in the WTO, the Members – and not the dispute settlement – should be the main actors in the development of the law. Limited judicial adjustment to new circumstances may be acceptable but the dispute settlement cannot become the route for the fundamental upgrading of the normative framework of the system, on pain of creating serious unbalances. As we are about to see, Appellate Body members, speaking or writing extra-judicially, have consistently shared this view.

<sup>11</sup> See, e.g. the seminal account by Federico Mancini, ‘The Making of a Constitution for Europe’ (1989) *Common Market Law Review*, 595-614.

<sup>12</sup> In other words, there is no way around the gap-filling that occurs with vague legal texts. There will always be gaps. But there are certainly different degrees of gap-filling, which can be more or less constrained.

<sup>13</sup> Joxerammon Bengoetxea, Neil MacCormick and Leonor Moral Soriano, ‘Integration and Integrity and Legal Reasoning of the European Court of Justice’, in Grainne De Burca and Joseph Weiler (eds.), *The European Court of Justice*, Oxford, Oxford University Press, 2001, p. 43, at p. 44.

<sup>14</sup> See Petros Mavroidis, *Dispute Settlement in the WTO: Mind over Matter* (2015), para. 5.4, noting that the Appellate Body was not heavily negotiated and was ‘more of an afterthought’: ‘The fact that only one article of the DSU is dedicated to the highest organ of dispute adjudication is proof enough that this has indeed been the case. ... The framers of the DSU paid little time in designing the entities that would adjudicate, but precious time in putting in place a system of compulsory third party adjudication’ (ibid.). See also Peter Van den Bossche, ‘From Afterthought to Centrepiece: the WTO Appellate Body and its Rise to Prominence in the World Trading System’, in Giorgio Sacerdoti, Alan Yanovic, and Jan Bohanes (eds.), *The WTO at Ten* (Cambridge: Cambridge University Press, 2006), pp. 289-325; Gabrielle Marceau (ed.), *A History of Law and Lawyers in the GATT/WTO – The Development of the Rule of Law in the Multilateral Trading System* (Cambridge: Cambridge University

view that deference and restraint become imperative. Therefore, in my view, adjudicating bodies in the WTO are not – and cannot be - ‘engines of change’,<sup>15</sup> as, for example, the European Court of Justice has often been, at times when the political arm of the EU was stalled.<sup>16</sup> Finally, the fact that, in the WTO, it is the Members, acting as Dispute Settlement Body (‘DSB’), that adopt the rulings and recommendations of the Panels and the Appellate Body (whilst, conversely, the latter simply ‘assist’ the DSB)<sup>17</sup> is symbolically and legally important.<sup>18</sup>

If this is correct, two corollaries should be put forward. First, the attitude and focus of the interpreter or adjudicator should be more on ‘discovering’ rather than on ‘inventing’ meaning (which is the key point of this paper). This is the essence of being simply agents with a limited mandate, and not principals crafting negotiating scenarios and possibilities. The panel in *US – Softwood Lumber IV* masterfully expressed this:

We consider that, if the Members feel the rules as laid down in the WTO Agreements do not address certain situations in what they consider to be a satisfactory manner, they should raise this issue during negotiations. Our task consists of interpreting the Agreement to explain what it means, not what in our view it should mean, nor are we allowed to read words in to the text of the Agreement which are not there, even if we were to consider that the text inadequately addresses certain specific situations.<sup>19</sup>

Former Appellate Body members have also insisted on this role of the WTO dispute settlement system. Writing in 2002, with considerations that are very much valid today, Claus-Dieter Ehlermann lucidly noted:

The WTO is characterized by an imbalance between the strong (quasi-) judicial structure set up by the DSU and the weak political decision-making process which is all too often blocked, between major trade rounds, by the traditional consensus rule. The work of panels and the AB would be facilitated if the political filters of the WTO, i.e., the committees established by different covered agreements, functioned better, and if the Ministerial Conference or the General Council were able to adopt interpretations and amendments, pursuant to Articles IX and X of the Marrakesh Agreement. Instead of

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Press, 2015).

<sup>15</sup> This *is* the main pressure on interpretation. What if there is need for change but, as I argue here, change cannot be accommodated by the law as it currently stands? Former AB Member Jennifer Hillman has commented as follows: ‘[i]n the absence of a legislative function waiting in the wings [the WTO is notorious for lack of legislative activity], judges often become very conservative, fearing to branch out very far since there is such a limited chance for timely course correction. Yet, this very real and understandable conservatism will come under ever increasing strain if cases come in areas in which there is little WTO law to apply, such as climate change or financial regulation, and little ability for the WTO to write new law in those areas if the negotiating process is not working efficiently’ (Jennifer Hillman, n. 6 above, 283).

<sup>16</sup> See Mancini, n. 11 above.

<sup>17</sup> See Article 11 of the DSU.

<sup>18</sup> Thus, though we live in a world of reverse consensus, strictly speaking, ‘judicial power’ still formally resides with Members (rather than with the Panels or the Appellate Body).

<sup>19</sup> Panel Report, *US – Softwood Lumber IV*, para. 7.60.

advocating mechanisms weakening the dispute settlement process, all efforts should be concentrated on strengthening the political arm of the WTO.<sup>20</sup>

This led him to conclude:

In view of the weakness of the political decision-making process, the responsibility of the AB is enormous. It must proceed with extraordinary circumspection and care. It is therefore advisable to pursue the cautious, case-specific approach that the AB has adopted in motivating its findings and conclusions.<sup>21</sup>

Secondly, adjudicators should not pay attention to pressures, expectations or vague legitimacy claims.<sup>22</sup> What they should care about, something for which they will never be censured, is the legality and correctness of their decisions.

The remarks above find confirmation in the rules on jurisdiction and interpretation that apply to the panels and the Appellate Body. These can be found in Article 3.2 of the Dispute Settlement Understanding that reads:

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, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.

The drafters of the Dispute Settlement Understanding have repeatedly referred to the ‘rights and obligations’ embodied in the covered agreements.<sup>23</sup> More specifically, they have expressly indicated that the dispute settlement system ‘serves to preserve’ these rights and obligations and that the latter also represent the limit of adjudication (it should be noted that even the Dispute Settlement Body – and not only the Panels and the Appellate Body assisting it – ‘cannot add to or diminish’ rights or obligations).<sup>24</sup> The fact that the drafters expressly – and repeatedly – introduced this language is significant.

Article 3.2 requires the dispute settlement system to ‘clarify’ WTO law by having recourse to the ‘customary rules of interpretation of public international law’. While to reference to the ‘clarification’ of the law simply reiterates the point just made, the reference to the use of the ‘customary rules of interpretation of public

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<sup>20</sup> Claus-Dieter Ehlermann, n. 6. For a discussion on the imbalance between judicial and legislative function in the WTO, see also Robert Hudec, ‘Free Trade, Sovereignty, Democracy: the Future of the World Trade Organization’ (2002) *World Trade Review*, 211-22.

<sup>21</sup> *Ibid.*

<sup>22</sup> See Luca Rubini, ‘The Good, the Bad, and the Ugly. Lessons on Methodology in Legal Analysis from the Recent WTO Litigation on Renewable Energy Subsidies’ (2014) *Journal of World Trade*, 895-936.

<sup>23</sup> See also Article 19.2 DSU on ‘Panel and Appellate Body recommendations’.

<sup>24</sup> The only route to changes of this type is treaty amendment (see Article IX of the Agreement Establishing the World Trade Organization).



international law' is arguably superfluous.<sup>25</sup> It is known that this expression has been intended to refer to the relevant provisions of the Vienna Convention on the Law of Treaties (VCLT; see Articles 31 to 33).<sup>26</sup> I will delve on these provisions in the next section. Suffice here to say that the principles of interpretation in these provisions put the treaty text at the center-stage of the hermeneutic activity of the interpreter. This is natural. It is the text that was negotiated and agreed. It is through the text that the parties expressed themselves and defined the contours of their rights and obligations. The text is both the starting point and the limit of interpretation.

It now looks clear how – through this approach to the interpretation and application of WTO law – the negotiators envisaged that the WTO dispute settlement system would provide 'security and predictability' to the multilateral trade system.

### 3. The crucial search for the 'negotiated balance' and its evidence

This section introduces two core concepts that will be used to enrich our analysis of subsidies case law.

#### *The concept of 'negotiated balance'*

The main thesis put forward in this paper is that, in interpreting WTO law, panels and the Appellate Body should search for the 'negotiated balance' of the rules they interpret. What the interpreter has to look for – always – is the equilibrium of the negotiated deal, what was agreed to (or was not agreed to) in its essence and, if possible, in its details. It is the identification of this balance that guides the act of giving meaning to a certain language or requirement in the treaties. This is a reflection of the contractual nature of WTO law underlined above. It is also, in my view, what former Appellate Body member James Bacchus expressed when saying that, in WTO law, the 'deal' is the

careful balance of rights and obligations of all WTO Members that was agreed in negotiating and concluding the treaty, and that is expressed in the words of the treaty and *only* in the words of the treaty.<sup>27</sup>

To perform this action of discovery of the negotiated balance, the customary rules of interpretation in international law are the necessary tools. The first paragraph of Article 31 of the VCLT, which lays down the 'general rule of interpretation', requires that

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

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<sup>25</sup> See Isabelle Van Damme, 'Treaty Interpretation by the WTO Appellate Body' (2010) *European Journal of International Law*, 605, at 608.

<sup>26</sup> Appellate Body Report, *US – Gasoline*, WT/DS2/AB/R, at 16-17; Appellate Body Report, *Japan – Alcohol*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, at 104; Appellate Body Report, *US – Softwood Lumber IV*, WT/DS257/AB/R, para. 59.

<sup>27</sup> Bacchus, note n 36 above, 512-513.

The text and the language of the treaty is thus at the center of the hermeneutic process. As noted above, this is obvious. It is through the text that the negotiating parties defined their rights and obligations. The meaning of the text should be arrived at also by considering the relevant context and the object and purpose of the treaty. It is known that, far from outlining a mechanic process or an exhaustive catalogue of rules of interpretation, Article 31 simply provides for some of the main principles of interpretation which should be considered together – holistically – to give meaning to a given language. In sum, the main evidence of the negotiated deal and the intention of the parties remains the text of the treaty, duly contextualized.<sup>28</sup>

Article 32 of the VCLT deals with the ‘supplementary means of interpretation’, reading:

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order or confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:

- (a) Leaves the meaning ambiguous or obscure; or
- (b) Leads to a result which is manifestly absurd or unreasonable.

Thus, after outlining the ‘general rule of interpretation’ in Article 31, the VCLT provides the interpreter with further tools to help her or him to give meaning to the treaty text. Although these rules, that give specific relevance to the negotiations and their context, have traditionally been given less weight than those of Article 31, they are important inasmuch as they help to complete or enhance the hermeneutic activity already conducted. It should also be noted that, like, in practice, a rigid separation between the various steps of Article 31 is not possible, the same could be said with respect to the relationship between Article 31 and 32.<sup>29</sup> The act of interpretation is a holistic process.<sup>30</sup>

Now, if there is admittedly nothing controversial about saying that panels and the Appellate Body should exercise their jurisdiction in the manner intended by the drafters, and that a proper reading of the VCLT seems to confirm that their hermeneutic efforts should always result in an interpretation that represent the deal that was negotiated,<sup>31</sup> it is a fact that it may not always be easy to find the negotiated meaning with precision.

Undoubtedly, in some cases, the lack of clarity or ambiguity of the law is simply justified by the fact that there was no agreement or, indeed, there was an agreement but to disagree. This results in what is called deliberate or creative

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<sup>28</sup> See Isabelle Van Damme, ‘Jurisdiction, Applicable Law, and Interpretation’ in David Bethlehem, Donald McRae and Rodney Neufeld, and Isabelle Van Damme (eds) *The Oxford Handbook of International Trade Law* (Oxford: Oxford University Press, 2009) 298, at 326 et seq.

<sup>29</sup> Finally, Article 33 deals with the interpretation of treaties authenticated in more languages.

<sup>30</sup> See Abi-Saab, n. 7 above.

<sup>31</sup> This, in my view, comes out from the following passage by former AB member, Abi-Saab, n. 7 above: ‘In practice ... much of the reasoning in interpretation is informed by the object and purpose, either consciously or subconsciously, where they can be identified, even though they many not figure explicitly as such in the analysis. Indeed, they are frequently disguised in the search for “*effet utile*”, or even the initial common intention of the Contracting Parties’.

ambiguity.<sup>32</sup> If this is the case, and in order to avoid undue gap filling or law making, the panel or the Appellate Body should arguably take - as highlighted by Claus-Dieter Ehlermann - the most circumspect and cautious approach permissible in the circumstances. This duty is not simply expressed by saying that the interpreter should respect the text of the covered agreements. It is much more than that. It more radically concerns the attitude of the interpreter that should make every effort in discovering meaning from the text, rather than imposing or inventing it. This is after all the deep meaning of the oft-repeated mantra (which is in fact a legal requirement)<sup>33</sup> that dispute settlement cannot add or diminish rights or obligations, and that the adjudicating bodies' mandate is simply one of 'clarification' of the law.<sup>34</sup> If the precise meaning of a certain provision or requirement may be elusive, what is sometimes less elusive is the (at least) general balance point the negotiators wanted to convey through the agreed text. This may refer to few basic elements where there was common ground. This balance, however general, can and should represent the main guiding principle for the adjudicator who shall then take position accordingly. Furthermore, if what the negotiators wanted, and indeed agreed to, may not be clear, it is sometimes easier to determine what they did *not* want to – the *outer boundaries* of the law.<sup>35</sup>

The gist of this approach is that the interpreter of WTO law should always seek what the negotiators meant, or, alternatively, could and would have meant, by including a certain legal requirement, using a certain language, resorting to a certain

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<sup>32</sup> As Richard Posner noted, '[d]eliberate ambiguity may be a necessary condition of making the contract; the parties may be unable to agree on certain points yet be content to take their chances on being able to resolve them, with or without judicial intervention, should the need arise. It is a form of compromise like "agreeing to disagree"' (see Richard Posner, 'Law and Economics of Contract Interpretation' (2004-2005) *Texas Law Review*, 1581, 1583). It is interesting to quote at this stage one passage from a recent article, written by three key actors in the negotiations of the Uruguay Round, and within it more specifically subsidy rules: 'These [WTO] Agreements had been negotiated with the GATT dispute settlement in mind; a system much less legalistic than the new one. Therefore, negotiators, sometimes deliberately, were creating some ambiguities in the negotiated texts or were defining certain issues in rather general terms, in the belief that no interpretation which had not been agreed by them could be imposed on them'. The final twist is telling: 'There is no doubt that had the negotiators known that their agreements would be submitted to as a legalistic system such as the present WTO dispute settlement, the Uruguay Round would have not been concluded or would have been concluded much later, after a long process of clarification of the new rules, their ambiguities and consequences'. Michael Cartland, Gérard Depayre and Jan Woznowski, 'Is Something Going Wrong in the WTO Dispute Settlement?' (2012) *Journal of World Trade*, 986. Pondering these statements, one could note that, already at the time of the Uruguay Round negotiations, GATT Panels were rather legalistic and rule-oriented in their approach. Equally, one wonders how different negotiating tables could be operating in 'clinical isolation' between each other.

<sup>33</sup> See Article 3.2 and 19.2 of the DSU.

<sup>34</sup> John Jackson once noted: 'arguably, [this language] resonates in the direction of a caution to the panels and appeal divisions to use "judicial restraint", and not to be too activist' *The World Trade Organization – Constitution and Jurisprudence* (London: Royal Institute of International Affairs, 1998), p. 91. One may even advance the idea that it is part of the duty of the adjudicator to simply acknowledge that there are possible gaps in the law, and that it is not for her or him, but for the legislator, to deal with them.

<sup>35</sup> I concur with Lorand Bartels when he suggests that, should the law be so indeterminate that no meaning can be identified, the panels and the Appellate Body would be discharging their duty to 'address' the relevant provisions and legal issues and 'assist' the Dispute Settlement Body, by simply making a statement to this effect. Lorand Bartels, 'The Separation of Powers in the WTO: How to Avoid Judicial Activism' (2004) *International and Comparative Law Quarterly*, 877. This would serve to highlight any lacuna in the law and shift the responsibility to those that are responsible for filling it – the Members.

legal architecture. If this is not possible, the concern should be to pinpoint what they could *not* and would *not* have meant. The interpreter cannot perform fundamental acts of reconstruction of the law. She or he does not have a completely clean sheet.<sup>36</sup> To say that the interpreter should look for the negotiated balance is also expressing an attitude towards the treaty text and its possible meaning. Once again: every effort should be made to discover (as opposed to impose) meaning out of the text under examination.

*Searching for evidence: the importance of the negotiating history and its context*

But what was the intention of the parties? The key issue then becomes how to establish what the negotiators and the drafters wanted. To what materials should Panels and the Appellate Body resort to find this intention? As noted, the main evidence of that intention remains the text of the treaty, but what if this is (as often happens) not conclusive?

As the VCLT warrants, the negotiating history and its context should play a role.<sup>37</sup> It is only through a careful analysis of the history of the negotiations and drafting of the legal text, that the interpreter can identify the balance of the legal disciplines.<sup>38</sup> The initial point of reference are therefore the negotiating documents that first and foremost can elucidate on the various positions and degree of agreement (or disagreement) reached between the parties and offer the necessary third dimension to the legal text. But the problem is that most negotiating documents often are unclear or, in any event, do not say anything about the intention of ‘all of the drafters’ as a collective unit. If anything, that should come out from the final treaty text. Most documents reflect the position of one or more parties and can hardly be used as a basis for proof of the intention of all the drafters.<sup>39</sup> What they may be useful at,

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<sup>36</sup> I believe that the same ethos comes out from the writing of several AB members when they are at pains to highlight their ‘circumspection and care’ in interpreting WTO law. They invariably refer to the importance of a textual approach (see Claus-Dieter Ehlermann, n. 20 above, 615-616), of the ‘trust in the written words’ because ‘words matter. So words must have meaning. ... The Members of the Appellate Body trust in words also, and, not least, because the Members of the WTO have clearly told them to do so. ... are of the view that the Members of the WTO meant what they said when putting words into the WTO treaty’ (James Bacchus, ‘Appellators: the quest for the meaning of *and/or*’ (2005) *World Trade Review*, 509-511).

<sup>37</sup> The views expressed extra-judicially by AB Members are mixed in this respect. The ‘low value’ attributed to the *travaux préparatoires* is generally justified by the ‘lack of reliable sources, and the ambiguities resulting from the presence of contradictory statements of the negotiating parties’ (see Claus-Dieter Ehlermann, n. 20 above, 616; see also Bacchus, n. 36 above, 506). But the fact that this is not an objection in principle but a practical consideration is confirmed by the suggestion that WTO Members should write a ‘common and official negotiating history’ of the pending Doha Development Round (Bacchus, n. 36 above, 521). The significance of preparatory works, that are ‘sometimes overlooked’, and of what negotiators meant to convey has also been very recently reaffirmed by current AB Member Thomas Graham, n. 6, above.

<sup>38</sup> This is leading the Court of Justice of the European Union to increasingly rely in certain areas on *travaux préparatoires* of legislation, especially those that are publicly available. See the interesting analysis by Koen Lenaerts, the current President of the Court of Justice of the European Union, in Koen Lenaerts and José Gutiérrez-Fons, *To Say What the Law of the EU Is: Methods of Interpretation and the European Court of Justice*, AEL 2013/9 Academy of European Law Distinguished Lectures of the Academy, at pp. 19-24.

<sup>39</sup> For a detailed analysis of the role of negotiating history in interpretation see Isabelle Van Damme, *Treaty Interpretation by the WTO Appellate Body* (Oxford University Press, 2009), chapter 8.

however, is in helping (at least) to identify the, even conflicting, terms of the discussions, their outer boundaries. Most importantly, whatever the informative value of the negotiating documents may be, it may be necessary to consider the ‘surrounding circumstances’ of the negotiations.

This way of proceeding is reflected in Article 32 of the VCLT which, as noted, is not simply about the use of the *travaux préparatoires*. This provision rather refers to the ‘supplementary means of interpretation, which include (*but certainly are not limited to*) the ‘preparatory work of the treaty and the circumstances of its conclusion’.<sup>40</sup>

Thomas Graham, one of the current Appellate Body members, thus recently noted:

A helpful record of the preparatory work often may not be available. So what help are “the circumstances of its conclusion” for checking or confirming an interpretation that we’ve given to a WTO agreement? What were those circumstances, and which are relevant?<sup>41</sup>

What could these circumstances be? One has to look for the broader diplomatic, political and economic context within which the negotiations took place and the negotiators operated.<sup>42</sup> The examination of the main issues that were relevant in the build-up of the negotiations and during them is the starting point. The second step is the reconstruction of the main, prevailing positions vis-à-vis those issues, as reflected, for example, in the domestic laws, litigation, official speeches, policy and academic literature. All these investigations have always to be set against what actually happened in the negotiations and is, despite its deficiencies, reported in the *travaux préparatoires* - and, eventually, what could be reflected (or not) in the treaty text.

Certainly, legal interpretation does not require adjudicators to become historians. But, much as historians can make reference to various sources (such as diaries or memoirs) and make use of them to give meaning and interpret historical events, I do not see any legal obstacle,<sup>43</sup> or any reason why even adjudicators should not decide to enrich their toolbox and, for example, use the most authoritative historical works or commentaries that can provide additional depth to the context of the negotiations. As Van Damme perceptively notes, it is often more an issue of evidence than of interpretation.<sup>44</sup> Thus the question is certainly not *what* may be used but *how* it can be used.<sup>45</sup>

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<sup>40</sup> Also the ‘subsequent practice’ of the parties that, within the framework of the Vienna Convention is considered ‘together with the context’, can play a role in giving meaning to the negotiated balance.

<sup>41</sup> Thomas Graham, see n. 6 above.

<sup>42</sup> The Appellate Body has treated this as context rather than as a supplementary means of interpretation. *EC – Chicken Cuts*.

<sup>43</sup> As just noted, the VCLT is certainly not an obstacle to the suggested practice.

<sup>44</sup> Isabelle Van Damme, note 39 above, p. 353: ‘these principles [of interpretation] are as much about evidence and burden of proof as they are about treaty interpretation’.

<sup>45</sup> If reference is made to scholarship, the main question then becomes to aptly separate (when this is possible) the reconstruction of a factual record of what happened in the negotiations (which we could tag ‘objective narrative’), which may be relevant, from the more subjective assessment of that factual record (the ‘subjective narrative’), which may be less relevant.

Incidentally, the time is ripe to highlight a paradox here. It is still not clear to me why, despite the obvious importance of identifying the negotiators' intention and the context of the negotiations, with very limited exceptions, WTO dispute settlement bodies are reluctant to cite literature (while it is common knowledge they use it, or heavily rely on it in their work). Would it really be completely inappropriate to rely on classic accounts such as the works of John Jackson, Bob Hudec or Kenneth Dam? Or, in the specific area of subsidies, the still highly relevant and fresh analyses of those actors and commentators who were writing during, or in the immediate aftermath of, the negotiations?<sup>46</sup> Are we sure that, discounted any known biases, the knowledge and awareness, the sense and sensibility of these people are of no use at all when it comes to making legal sense of GATT and WTO laws and, going back to the claim of this paper, detecting the 'balance point' of the disciplines?<sup>47</sup> It is known how in these papers negotiators elucidated and summarised their positions and scholars reacted to them. These pieces constitute an important body of literature that constitutes evidence of the context and circumstances of the negotiations. If literature coeval to the negotiations may be particularly relevant, more contemporary analysis may be valuable too. Serious historical studies on the GATT and the WTO, carried out with strong methodology and with access to several sources, are increasingly common.<sup>48</sup> Shall we simply ignore them once we enter the doors of the temple of WTO dispute settlement? Or, rather should we welcome and promote this type of scholarship and underline its practical relevance? Again – I have not heard or read any plausible explanation of why the WTO wants to be (or to appear?) virtually and completely immune to serious scholarly work.

Finally, at the risk of stating the obvious, it is clear that the 'negotiated balance' in the relevant laws will not come out – as such - from the negotiating documents (or the most authoritative commentary). In other words, it is always the interpreter–adjudicator who is in the driving seat and has to make full sense of all the evidence available, put it into its context and make use of her or his logical ability to carry out the act of interpretation., and to carry out the act of interpretation – which, as Lord McNair once said – is more an art than a science.<sup>49</sup>

#### **4. The interpretative attitude of the Panels and Appellate Body in subsidy cases**

This section outlines the key questions of the paper and provides the reader with a brief conceptual roadmap.

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<sup>46</sup> The list is very long. I include only a few names here: Gary Horlick, Peggy Clarke, Judy Bello, Mike Levine, Alan Holmer, Dan Hunter, Susan Haggerty, John Greenwald, Gerard Depayre, Mauro Petriccione, Gary Hufbauer, Joanna Shelton-Erb, Richard Diamond, Terry Collins-Williams, Geny Salembier.

<sup>47</sup> Suffice it to read Article 38(1)(d) of the Statute of the International Court of Justice which reads that the ICJ is also to apply 'judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law'. It is also known that, in the EU law practice, academic scholarship is widely used. One good example is given by the Opinions of the Advocates General to the Court of Justice of the European Union, which are replete with academic citations.

<sup>48</sup> See, for example, Irwin, Mavroidis, Sykes, *The Genesis of the GATT* (Cambridge: Cambridge University Press, 2010).

<sup>49</sup> Ian Sinclair, *The Vienna Convention on the Law of Treaties* (Manchester: Manchester University Press, 1984) 118. See also Neville Brown and Francis Jacobs, *The Court of Justice of the European Communities* (5<sup>th</sup> edition, London: Sweet and Maxwell, 2000) 323.

Against the paradigmatically unclear regulatory framework of the SCM Agreement, what was the attitude of the panels and the Appellate Body towards treaty interpretation in these first twenty years? In particular, is there a difference between the approach of panels and that of the Appellate Body? Can we identify different phases, in particular more self-restrained periods or more activist approaches to the law? Has one clearly given way to another? Or are trends difficult to detect?

As regards the first question, this paper assumes that more consistency, or indeed an evolution, can more easily be found in the case-law of the Appellate Body than for the panels. The Appellate Body is a permanent body and, although it sits in three-member divisions, there is known to be a considerable degree of collegiality in the deliberation of each case, with meetings extended to non-division members and opinions sought from them,<sup>50</sup> all to the benefit of consistency of jurisprudence (and partly compensating for changes in composition). Moreover, it benefits from the support of a dedicated and separate secretariat. By contrast, panels are established on an ad hoc basis. Panelists differ in terms of their expertise and knowledge of trade law.<sup>51</sup> The WTO Secretariat certainly plays a supporting and possibly a unifying role in the panels' work but its impact on the actual decisions is not clear. In any case, even assuming there is a strong influence of the secretariat on the adjudicating process, it is difficult to identify its specific impact on particular cases or issues. And it is equally difficult to speculate on whether, within the specific context and design of WTO dispute settlement (with the above-mentioned two-tier adjudicating system), it is reasonable to expect that the panels' attitude tends to be restrained rather than activist.

For these structural reasons, it is more difficult to identify a 'panels' jurisprudence' and assess whether it evolves or changes. By contrast, the Appellate Body's work is more naturally suited to constitute 'jurisprudence' and can be scrutinized. The reader should bear this caveat in mind.

During the past twenty years, the WTO dispute settlement system has produced 81 decisions on subsidies on industrial goods only (not agriculture), issuing 96 reports. In this paper, we review 24 of those reports (some directly, and others, dealing with the same issues in other cases or in the same cases in the first instance, indirectly). These cases have been selected because they focus almost exclusively on substantive issues, mostly related to the definition of 'subsidy', have (almost all) attracted significant attention and, in some cases, generated controversy. Chronologically these reports are evenly spread during the period of 1999 to late 2014 (see Table 11.1).<sup>52</sup> Although this review is not complete, and there are notable omissions,<sup>53</sup> this selection is sufficiently representative and comprehensive to identify directions and trends in subsidy jurisprudence.

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<sup>50</sup> See Rule 4(3), and also Rule 4(1), of the Working Procedures of the Appellate Body.

<sup>51</sup> Which has led many to advocate the creation of a permanent panel system.

<sup>52</sup> Seventeen out of those 24 reports were adopted during first ten years of dispute settlement activity. This predominance is, however, fully in line with the fact that 66% of the WTO disputes took place during that period. See Petros Mavroidis, *Dispute Settlement in the WTO: Mind Over Matter* (2016), at para. 5.3.

<sup>53</sup> Most importantly, *EC – Sugar* (265, 266, 283) and *US - Cotton* (267), adopted in 2004 and 2008, which, despite their huge importance, did not raise any significant definitional issue. The absence of the reports in *EC – Aircraft* (316) and *US – Aircraft* (353), which were initiated in 2004 and are still

**Table 1 - disputes and reports reviewed**

Year	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total
Panel				3		2	1	1		3					1		2		1	14
Appellate Body				1	2		2		1	1						1		1	1	10

I analyse these reports by dividing them into two groups: the ‘jurisprudence of discovery’ and the ‘jurisprudence of invention’. These refer to those decisions where the Panels and the Appellate Body respectively have, or have not, searched and found the ‘negotiated balance’ underlying the provisions at issue. After analyzing each group, I will provide a more general assessment.

### 5. The ‘jurisprudence of discovery’: when the WTO dispute settlement gets it right

In this section, I single out a few decisions, spanning from 1999 to 2012, which, in my view, represent true turning points in the creation of the *acquis* on subsidy laws. They all focus on definitional issues, which, for its intricate interplay of technical and policy issues, is the real testing ground of any effort at adjudication of subsidy rules.<sup>54</sup> All these cases can be grouped under the term ‘jurisprudence of discovery’ because they involved panels and the Appellate Body discovering the essence of the balance of the subsidies disciplines which were negotiated and agreed upon during the Uruguay Round.

Three key concepts emerge. The first is the *market-orientation* of the definition of subsidy that, conversely, also means that non-market (read: policy) considerations are not taken into account. The second notion relates to the inevitable *formalism* and, to some extent, *simplicity* of the type of assessment required for defining what is a subsidy. The third concept is the importance of the fact that subsidy laws, in particular the rules determining their material scope, are often the result of a delicate balancing of the different positions prevailing during the negotiations. As will be seen, there is indeed a *balance* point between conflicting forces and even goals that the definition has to satisfy.

#### *Canada — Measures Affecting the Export of Civilian Aircraft (Canada – Aircraft)* (DS 70)

Both the Panel and the Appellate Body in *Canada – Aircraft* were called upon to interpret the term ‘benefit’, which is one of the two prongs of the definition of

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pending, is important but any significant analysis of the issues raised in those cases would have demanded much more space. Finally, disputes raising important procedural or remedial issues, such as *Australia – Leather* (21.5), are also excluded.

<sup>54</sup> As a result of this, by far the large majority of subsidy cases have raised important questions about Article 1 of the SCM Agreement, to an extent that is probably not comparable to what has happened with respect to definitions under other covered agreements. The main reason is that key concepts of the definition of subsidy, such as the requirement that a ‘benefit is conferred’, can more easily open up to policy considerations. See Luca Rubini, note n. 22 above, p. 923.



subsidy. Under Article 1 of the SCM Agreement, for a subsidy to exist there must be one of the specific forms of financial contribution outlined therein or, alternatively, any form of income or price support, and either of this should confer a benefit.<sup>55</sup> Both the Panel and the Appellate Body found that whether the governmental action at issue confers a benefit (or not) depends on the ‘marketplace’. This is ‘an appropriate basis for comparison’ (Appellate Body)<sup>56</sup> or, with even firmer language, ‘the only logical basis’ (Panel).<sup>57</sup>

Those findings reflect the choice for a progressive construction of WTO subsidy laws on the basis of the main concern subsidies may cause for the trading systems, i.e. the potential to cause distortions and spillovers. To put it another way, subsidies cause apprehension and are an issue for the trading system because they may distort the market (although, crucially, they may often correct it - but this is a separate issue and does not represent the key rationale for regulating subsidies in a multilateral trading system).<sup>58</sup> Viewed from this perspective (i.e. the potential to distort trade and competition), it is then clear why the Panel and the Appellate Body applied the same approach, not only in terms of outcome, but also virtually using the same language.<sup>59</sup> The point I am making is fully clear if we consider the oft-repeated passage from the Appellate Body report:

The marketplace provides an appropriate basis for comparison in determining whether ‘benefit’ has been ‘conferred’, because the trade-distorting potential of a ‘financial contribution’ can be identified by determining whether the recipient has received a ‘financial contribution’ on terms more favourable than those available to the recipient in the market.<sup>60</sup>

This reference to the market is not always fully appreciated. It is true that there are difficulties in identifying and quantifying a precise benchmark against which the

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<sup>55</sup> Article 1.1 reads: “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);  
(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.”

<sup>56</sup> Appellate Body, *Canada – Aircraft*, para. 157.

<sup>57</sup> Panel, *Canada – Aircraft*, para. 9.112.

<sup>58</sup> See Luca Rubini, *The Definition of Subsidy and State Aid: WTO Law and EC Law in Comparative Perspective* (Oxford University Press, 2009), chapter 2.

<sup>59</sup> Compare, Appellate Body, para. 157, and panel, para. 9.112. It is also important to note that this anchorage to the marketplace is found in many other panel and Appellate Body reports passed subsequently, which are not included in this brief review.

<sup>60</sup> Appellate Body Report, para. 157.

governmental action has to be tested.<sup>61</sup> Markets are complex, actors do not always act as expected (ie rationally) and governmental intervention in the economy can seriously distort the working of market forces.<sup>62</sup> Some thus suggest that the assessment would only constitute ‘market mimicry’<sup>63</sup> or could only work if resort is made to ‘fictions’.<sup>64</sup> While not negating these obvious difficulties,<sup>65</sup> it is clear that the market is the place where trade and competition occur, and which is impacted by public action in the form of subsidies. It is therefore inevitable to look for benefit benchmarks there. In this sense, the market is much more than a paradigm in the benefit benchmarking and more generally as a key test to assess trade distortions in subsidy laws. It is a common sense and logical necessity.<sup>66</sup>

*United States — Tax Treatment for “Foreign Sales Corporations” (US – FSC) (DS 108)*

Through four reports between 1999 and 2002, *US – FSC* provided the opportunity to gain a better understanding of the test to establish when the government is not acting in the economy as a market operator (for example by investing or lending) but as a sovereign, through taxation. The predominant legal criterion to establish whether a tax measure is a subsidy is whether the government foregoes, or does not collect, revenue ‘otherwise due’.<sup>67</sup>

At issue, first in the original and then in the implementation proceedings were two US statutes (the Foreign Sales Corporation Act and Extra-Territorial Income Act) that essentially exempted a portion of the income earned outside the US by certain qualifying companies from taxation. Crucially, both statutes derogated from the principle of ‘world-wide taxation’ which prevails in US tax law and which taxes worldwide income earned by residents. Other countries, and in particular European countries, adopted the principle of territoriality, whereby only the income earned in the territory (by both residents and non-residents) is taxed. The US move was justified by the need to redress the competitive disadvantage that US multinationals were allegedly suffering vis-à-vis their European competitors. Indeed, from an *economic* perspective, the broader scope of application of worldwide systems, with the associated disincentive to exploit the opportunities of low-tax jurisdictions, seems to

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<sup>61</sup> Moreover, another line of criticism attacks the reference to the market because it would not take into account the crucial determinant of public intervention in the market, i.e. the public interest. For a full discussion see, Rubini, n. 58 above, 252-259.

<sup>62</sup> See the perceptive analysis of Alan O Sykes, ‘The Questionable Case of Subsidy Regulation: A Comparative Analysis’ (2010), *Journal of Legal Analysis*, 473-523.

<sup>63</sup> Dan K. Tarullo, ‘Beyond Normalcy in the Regulation of International Trade’ (1986/1987) *Harvard Law Review*, 546, 570-579.

<sup>64</sup> Andrew Lang, *Governing ‘As If’: Global Subsidies Regulation and the Benchmark Problem* (May 4, 2014). LSE Legal Studies Working Paper No. 12/2014 (<http://ssrn.com/abstract=2432642> or <http://dx.doi.org/10.2139/ssrn.2432642>).

<sup>65</sup> For a full analysis of these issues see Luca Rubini, *The Definition of Subsidy and State Aid: WTO Law and EC Law in Comparative Perspective* (Oxford University Press, 2009), chapter 8.

<sup>66</sup> It should be clear that I am not advocating here the use of a paradigmatic and pure market benchmark. I am simply referring to the market and its conditions at the time when the government actually intervenes with the measure that is under examination. Furthermore, one key inevitable corollary of the market-orientation of the benefit analysis is that the policy motivations of government action have not been traditionally considered at this level. See Rubini, n. 58 above, chapter 8.

<sup>67</sup> See Article 1.1(a)(1)(ii) of the SCM Agreement.

put US groups at a disadvantage in international activities compared to European groups. Through ingenious transfer-pricing, the latter could move even very sizeable portions of their income to off-shore jurisdictions and eventually pay no tax at all, anywhere. The economic goal and effect of the US statutes under review were to re-balance the playing field.

Two panels and the Appellate Body twice provided arguably four different tests and gave some meaning to the expression ‘otherwise due’.<sup>68</sup> Through these tests, they all essentially rebuke the US practice of maintaining a broader general rule and then introducing selective exceptions for certain firms. What the US was doing through the Foreign Sales Corporation Act first and the Extra-Territorial Income Act afterwards was foregoing revenue that would have been otherwise due— i.e. in the absence of those two legislative measures and in the light of the prevailing principles of US tax law.

The reports highlight the difference in approach between legal and economic analysis.<sup>69</sup> In my view, these rulings are formally and even substantially correct - certainly in legal terms, although maybe not in terms of economic logic. This formalism, this rigidity (and lack of sensitivity towards any compensatory logic: remember: the US tax measures had been introduced to level – and not to tip – the playing field) is correct.<sup>70</sup> It is much more in line with the idea that the WTO agreement is a contract and that the dispute settlement system is simply ensuring that it is respected, than a different approach that would have done justice to the ultimate policy objectives of the US and the simply compensating effect of its tax exemption.<sup>71</sup> In other words, the issue was simply whether the US measures did or did not constitute a subsidy, and not whether this policy of support was desirable or legitimate (which is, both conceptually and practically, a separate question).

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<sup>68</sup> See Panel Report, paras. 7.43-7.46; Appellate Body Report, paras. 90-91; Panel Report (Article 21.5 DSU), paras. 8.14-8.30; Appellate Body Report (Article 21.5 DSU), para. 91. These four tests are discussed in Luca Rubini, n. 58 above, chapter 9.

<sup>69</sup> Petros C Mavroidis, *Trade in Goods*, footnote 27 to page 534, underlines that the ‘rationale’ behind the US law is ‘immaterial’. See also Robert E Hudec, ‘Industrial Subsidies: Tax Treatment of ‘Foreign Sales Corporations’’ in Ernest-Ullrich Petersmann and Mark A Pollack (eds) *Transatlantic Economic Disputes - The EU, the US, and the WTO* (Oxford: Oxford University Press, 2003) 175.

<sup>70</sup> Formalism is not necessarily negative. It is in the nature of the law to often rely on ex ante and pre-made assessments that take the shape of ‘per se’ rules like presumptions. In other words, the value that the law brings in these cases is that the rules of the game are settled for a certain period of time and that renegotiation (with its costs and uncertainty) is not possible. The only issue is whether this normative approach is appropriate to achieve the goal of the provision and that any relevant under- or over-inclusion is tolerable. If not, the system should design the rule as a ‘standard’, continuously attuned to the factual circumstances in the context of an individual assessment. See Luca Rubini, ‘The Good, the Bad, and the Ugly. Lessons on Methodology in Legal Analysis from the Recent WTO Litigation on Renewable Energy Subsidies’ (2014) *Journal of World Trade*, 895-938, footnote 103 to page 104: ‘Note that there is nothing ontologically wrong with formalism, or conversely inherently right with “substantialism”’. The important points to have in mind are both the practical nature of law – law has to be applied to certain conducts and events – and the objectives of the specific discipline at hand. This double analysis will tell whether, in the specific circumstances, it is better to have a rule requiring a formal or a substantial analysis’.

<sup>71</sup> Ironically despite the initially neutrality of WTO law with respect to tax decisions, the dispute settlement rulings ultimately force countries to choose certain tax systems. The negative integration nature of the WTO agreement – WTO law cannot impose a choice of tax system – gives way to the responsibility of countries to abide fully by the contract they have signed.

*United States — Measures Treating Export Restraints as Subsidies (US – Export Restraints) (DS 194)*

The third dispute is *US – Export Restraints* which was decided in 2001 by a panel decision only. This is probably the **most important report** relating to subsidy laws.<sup>72</sup> This is a landmark decision because it casts light on both the function and interpretation of the requirement of the existence of a financial contribution, and represents the prototype of the correct approach to WTO law. The main issue was whether an ‘export restraint’ could constitute a financial contribution in the form of a government-entrusted or government-directed provision of goods in the sense of Article 1.1(a)(1)(iii) and (iv) of the SCM Agreement.<sup>73</sup>

In response to the effects-based (and hence informal) approach advocated by the US, the panel underlined that the determination of whether a financial contribution exists must concentrate on the examination of the nature of the action by the government (read: form) and not on its effects (and, I would add, its objectives).<sup>74</sup> A different interpretation whereby, irrespective of its nature, any governmental action producing a certain ‘subsidy-like’ result would effectively amount to a financial contribution, would eventually mean reading the requirement of a financial contribution out of the definition of a ‘subsidy’ and leaving dangerously open the notion of subsidy and the application of the rules. According to the panel, the focus of the financial contribution assessment must therefore be on the government’s action rather than its possible effects on, or the reactions of, those specifically affected, even if those effects or reactions can be expected.

The financial contribution requirement plays a crucial *limiting* role within the context of subsidy rules. In this light, the panel went on to clarify the function of the fourth subparagraph of the Article 1.1(a)(1) of the SCM Agreement, which applies where the governments act indirectly through a private body that has been entrusted or directed to carry-out one of the three exhaustive forms of financial contribution. According to the panel, the objective of this fourth subparagraph is certainly not to extend the coverage of the definition of subsidy (by adding new forms of public action to those already listed), but rather to act as a crucial anti-circumvention device and avoids the risk that a government could jeopardise the effectiveness of the discipline by acting through a private body.

Once again, we notice a discrepancy between this legal (and formal) approach and an economic approach based on the effects. What matters is whether a certain

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<sup>72</sup> A full analysis can be found in Luca Rubini, *The Definition of Subsidy and State Aid: WTO and EC Law in Comparative Perspective* (Oxford: Oxford University Press, 2009), chapter 4. A couple of significant biographical circumstances explain the special position of the panel. The first relates to the composition of the panel, which was chaired by Michael Cartland, the diplomat largely responsible for negotiations of the SCM Agreement. The Rules Division of the Secretariat, which supported the Panel, was chaired by Jan Woznowski who, during the Uruguay Round negotiations, assisted Cartland in the subsidies negotiations and, in particular, in drafting various iterations of the Chairman’s texts. All this gave a comprehensive insight into the delicate negotiations of the notion of subsidy and of the spirit of the delicate balance reached in the final agreement, and probably also goes some way in explaining why there was no appeal.

<sup>73</sup> See Panel Report, paras. 8.15-8.76.

<sup>74</sup> See n. 66 above.

measure belongs to one of those that the drafters wanted to be covered by the definition of subsidy and this irrespective of whether *other* measures producing similar or identical effects are left out. The findings of the panel are crucial, and should be positively welcomed. They focus on the inner logic between the various parts of the definition of a ‘subsidy’, and, in doing so, also recognise the role of the definition, which is to distinguish what should and should not be regulated by the disciplines of the SCM Agreement. We may disagree on how well or how appropriately the boundaries of the definition of subsidy are set (what they do is to go some way towards leaving ‘regulatory acts’ out of the concept of subsidy) – and maybe, with the benefit of hindsight, even the same drafters may have misgivings – but, to opine otherwise and enlarge the definition too much, would fundamentally disregard the function of the financial contribution requirement and ultimately of the notion of subsidy. It would disregard its balance.

*China – Countervailing and Anti-Dumping Duties on Grain Oriented Flat-rolled Electrical Steel from the United States (China – GOES) (DS 414)*

The Panel in *China – GOES* adopts the same ethos and the same findings as the panel in *US – Export Restraints*, with respect to the phrase ‘any form of income or price support’ of Article 1.1(a)(2) of the SCM Agreement.

The Panel found that the concept of ‘price support’ involves the direct ‘setting and maintaining’ of a price. However, it does not cover a random change in price that is merely a ‘side-effect’ of a government measure. The concepts of ‘income’ and ‘price support’ must thus be interpreted as being influenced by the same spirit of the financial contribution requirement, i.e. not every government measure that produces certain subsidy-like effects is covered. It follows that the focus is more on the nature (read: the form) of the government action than simply on its effects or objectives. This means that, despite its potentially broad scope, Article 1.1(a)(2) covers those types of governmental conduct that raise ‘price’ or ‘income’ in a direct and immediate way.

Our (positive) assessment of this case is the same as that of *US – Export Restraints*.

**6. The ‘jurisprudence of invention’: when the WTO dispute settlement gets it wrong**

Other reports, which also relate mostly to definitional issues, do not contribute to the proper understanding of WTO subsidy laws. Testing them against the benchmark of whether they capture and reflect the negotiated balance of the relevant provisions, I divide them in three categories: those that raise serious doubts about their correctness, those that are wrong and those that are arguably seriously wrong.

*United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom (US – Lead Bars II) (DS 138) and United States – Countervailing Measures Concerning Certain Products from the European Communities (US – CVDs on EC Products) (DS 212)*

In these disputes, which took place from 1999–2000 and 2002–2003, first the panels and then the Appellate Body were confronted with the issue of the effects of privatisation on prior subsidisation. In particular, should an arm's length sale for a fair market value and in compliance with normal market conditions extinguish the benefit of the subsidy received by the seller?

The US had imposed countervailing duties on imports produced by companies that, before being privatized, had received subsidies. The US crucially argued that the circumstances of the privatization, and in particular whether the company or its assets had been transferred under commercial terms, were irrelevant and that what mattered for subsidy laws was the continuance of the productive operations. In both cases, however, the focus of the panels and the Appellate Body differed from the US. Their key focus was on the change in ownership and its conditions, and in particular on their compliance with a market benchmark. They thus both concluded that the payment of a 'fair market value' was capable of excluding that the buyer had benefited from the transaction.<sup>75</sup>

These decisions have been strongly criticised on the grounds that the adjudicating bodies completely neglected that the requirement at issue was whether a benefit continues to exist.<sup>76</sup> The price paid for the firm and the financial wealth of its owners is irrelevant in this respect. What counts is whether the competitive position of the firm *continues* to be advantaged even after the transaction.<sup>77</sup> By being economically ill informed, these rulings are therefore not correct.

*United States – Final Countervailing Duty Determination with respect to certain Softwood Lumber from Canada (US – Lumber IV) (DS 257)*

In this dispute from 2004, one of the key questions was how to define the appropriate market benchmark when there has been a significant commercial presence of the government in the market. In these circumstances, is the market distorted? If so, is it possible to refer to reliable commercial benchmarks?

The US Department of Commerce (DOC) had found that, by granting the right to harvest timber on Crown Land, Canada was providing a financial contribution in the form of provision of goods (under Article 1.1(a)(1)(iii) of the SCM Agreement) to lumber producers. The issue was whether these goods were also provided at less than

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<sup>75</sup> In *US – CVDs on EC products*, there was some variance between the Panel, which established an absolute presumption of extinction of the benefit, and the Appellate Body, which was more cautious and, after underlining the ability of governments to direct privatisations so as to 'influence the circumstances and conditions of the sale', underlined that no automatic presumption is acceptable and the need for a case-by-case analysis.

<sup>76</sup> Gene Grossman and Petros C Mavroidis, 'Here Today? Gone Tomorrow?' in Henrik Horn and Petros C Mavroidis (eds) *The WTO Case Law of 2001* (Cambridge: Cambridge University Press, 2003), 170; id, 'Recurring Misunderstandings of Non Recurring Subsidies' in Henrik Horn and Petros C Mavroidis (eds), *The WTO Case Law of 2002* (Cambridge: Cambridge University Press, 2005) 78; Richard Diamond, 'Privatization and the Definition of Subsidy: A Critical Study of Appellate Body Textualism' (2008) *Journal of International Economic Law* 649.

<sup>77</sup> While accepting the validity of this criticism, what remains to be seen is *where* in the SCM Agreement this 'competition' analysis should be more properly done – in the context of the benefit/definition or rather when adverse effects/injury are assessed. See Diamond, id, and Rubini, note n. 58 above, footnote 44 to page 349, for a full analysis of this point.

adequate remuneration thereby conferring a benefit pursuant to Article 14 (d) of the SCM Agreement. More specifically, subparagraph (d) of this provision reads:

the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined *in relation to prevailing market conditions* for the good or service in question *in the country of provision or purchase* (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).<sup>78</sup>

In its determination, the US DOC had found that the prices of private timber sales in Canada did not represent a commercial market baseline because they were distorted by government intervention. In particular, the supply of ‘public’ timber was so dominant in the market that the prices of the few private suppliers were not determined independently but were necessarily depressed and aligned to the lower level of governmental prices. Since these prices were not reliable, the US DOC used the prices of stumpage in certain bordering states in the north of the US as a benchmark, making adjustments to account for differences in conditions between those states and Canadian provinces.

But – importantly – was it legitimate to look outside the ‘country of provision’, as the letter of the law clearly stated, in the search for appropriate benchmarks?

The Panel found that ‘prevailing market conditions’ refer to the market conditions ‘as they exist’ or ‘which are predominant’ in the country of provision.<sup>79</sup> Thus, the US’ argument that the term ‘market’ means ‘fair market value’ or market ‘undistorted by government intervention’ was rejected.<sup>80</sup> In particular, the Panel underlined that, ‘as long as there are prices determined by independent operators following the principle of supply and demand, even if supply or demand are affected by the government’s presence in the market, there is a “market” in the sense of Article 14(d) [of the] SCM Agreement’.<sup>81</sup>

Crucially, the Panel, while appreciating the ‘economic logic’ of the US’ argument, considered it to be impossible – against the express and clear text of Article 14(d) – to ‘substitute its economic judgment for that of the drafters’ of the SCM Agreement.<sup>82</sup> In these circumstances, the only usable benchmarks should have been found *within* – and not outside – the country of provision.

The Appellate Body, however, took a different view. The Panel’s interpretation was ‘overly restrictive’ and, in some cases, the prices of the ‘country of provision’ many not be informative. This required consideration of alternative

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<sup>78</sup> Emphasis added.

<sup>79</sup> Panel Report, para. 7.50. A similar finding was made by the previous Panel in *US – Lumber III*, para. 50.

<sup>80</sup> Panel, *US – Lumber IV*, paras. 7.50-7.51.

<sup>81</sup> *ibid*, para. 7.60.

<sup>82</sup> *ibid*, para. 7.59.

benchmarks rather than the private prices in the country of provision, if the purposes of Article 14(d) of the SCM Agreement ‘are not [to be] frustrated’.<sup>83</sup>

The reasoning of the Appellate Body has been criticised for being too liberal and too far from the text of the provision at issue.<sup>84</sup> This is a clear instance of interpretation plainly *contra legem*.

*United States — Countervailing Duty Investigation on Dynamic Random Access Memory Semiconductors (DRAMs) from Korea (US – DRAMS) (DS 296)*

In 2005 the Appellate Body was called upon to interpret, once again, the meaning of the terms ‘entrust’ and ‘direct’ of subparagraph (iv) of the financial contribution requirement. Since the panel report in *US – Export Restraints*, there had been a few cases in which panels had adopted a progressively more flexible interpretation of those terms. Thus, whereas the Panel in *US – Export Restraint* had concluded that the ordinary meaning of the concepts of ‘entrust’ and ‘direct’ necessarily conveyed an idea of ‘explicit and affirmative action [of] delegation or command’, the panels in *US – DRAMS (DS 296)*, *Korea – Commercial Vessels (DS 273)* and *EC – DRAMS (DS 299)* relaxed those standards a bit. They agreed that the terms ‘entrust’ and ‘direct’ must respectively contain ‘an element of delegation or command’, and that they should invariably take the form of an ‘affirmative’ act. However, they disagreed as to whether these actions necessarily needed to be explicit insofar as they could be ‘explicit or implicit, informal or formal’.<sup>85</sup>

In *US – DRAMS*, the Appellate Body took a significant step further along this trajectory of relaxing the legal standard [of what]. It rejected the view that the concepts of entrustment and direction be limited to the notions of delegation or command. For example, in addressing the concept of ‘direction’, the Appellate Body found that this is connected with the exercise of governmental authority over a private body. ‘A “command” ... is certainly one way in which governments can exercise authority over a private body ... but governments are likely to have other means at their disposal to exercise authority over a private body’, some of which *are more subtle or may not involve the same degree of compulsion*.<sup>86</sup> Moreover, as regards the complexity of the act of entrustment or direction, the Appellate Body (unlike all previous panels) did not require that the action of the government be ‘affirmative’.

There is a concern that the Appellate Body’s interpretation of ‘entrust’ or ‘direct’ is too wide and vague and thus introduces a serious element of imbalance within the financial contribution requirement and the definition of a ‘subsidy’ as a whole.<sup>87</sup> The panel report in *US – Export Restraints* had made it clear that subparagraph (iv) of the financial contribution requirement performs two different –

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<sup>83</sup> Appellate Body, *US – Lumber IV*, para. 101.

<sup>84</sup> See, e.g., Henrik Horn and Petros Mavroidis, ‘United States – Final Determination with Respect to Certain Softwood Lumber from Canada (AB-2003-6, WT/DS257/AB/R)’ (2006) World Trade Review 130-145.

<sup>85</sup> Panel, *US – DRAMS*, para. 7.33; Panel, *Korea – Commercial Vessels*, para. 7.370; Panel, *EC – DRAMS*, para. 7.57.

<sup>86</sup> Appellate Body, *US – DRAMS*, para. 111.

<sup>87</sup> See Luca Rubini, n. 58 above, 113-115.



indeed opposing – functions. On the one hand, it does not widen the types of financial contribution covered. On the other hand, it operates as an anti-circumvention device. The main focus of the Panel in *US – Export Restraint* was to show that the financial contribution requirement *covers only* certain forms of public intervention. Hence, in this context, one can understand why the standards of imputability of the notions of ‘entrust’ and ‘direct’ were particularly rigorous. This changes with the subsequent cases. The role of delimitation of the financial contribution was no longer an issue. Consequently, the second purpose of subparagraph (iv) – ie the anti-abuse device – gains centre stage. It thus becomes important for the financial contribution requirement to catch practices that otherwise would escape the scope of the definition of subsidy. Consequently, the standards of imputability of ‘entrust’ and ‘direct’ are interpreted more generously.

The bottomline is that you always a need to strike the right balance between the two functions of subparagraph (iv) and that an unduly generous construction of its key legal requirement may risk enlarging unduly the scope of the financial contribution and thus of the definition of a ‘subsidy’. Arguably, this is what happened with the very flexible interpretation of the Appellate Body’s decision in *US – DRAMS*.

*United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China (US – AD/CVD) (DS 379)*

In 2011 *US – AD/CVD*, the Appellate Body similarly neglected the need for balance within the definition of a ‘subsidy’. Unlike the Panel,<sup>88</sup> the Appellate Body imposed a strict test for determining whether an entity is a ‘public body’. Under the prevailing case-law, public control on an organisation was necessary and sufficient to classify it as a ‘public body’.

The Appellate Body changed the game in *US – AD/CVD* and found that the notion of ‘public body’ does not simply refer to any entity controlled by a government. It refers, more specifically, to those entities that perform governmental functions, or are vested with and exercise the authority to perform such functions.<sup>89</sup>

Does this finding make it more difficult to qualify measures as subsidies? (A problem that, according to some, would be particularly acute with China because of the pervasiveness of state-owned enterprises in its economy.) An initial answer might be that, if such undertakings cannot be considered as public bodies, they would necessarily qualify as ‘private bodies’, for the purposes of Article 1.1(a)(1)(iv) of the SCM Agreement. It would thus be necessary to prove in each case that the conduct at issue had been ‘directed or entrusted’ to such a body, but, as we have just seen, after the *US – AD/CVD* case, the attribution of conduct to a government can more easily be established.<sup>90</sup>

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<sup>88</sup> And indeed in previous Panels’ decisions not considered in this review.

<sup>89</sup> See Appellate Body, *US – AD/CVD*, para 290.

<sup>90</sup> Hence – paradoxically - one lack of balance could remedy another possible lack of balance in the definition. This requires further explanation.

The definition of ‘entrust’ or ‘direct’ is not, however, the last step of the analysis. Subparagraph (iv) includes two final provisos that essentially require that the transaction at issue is ‘normal governmental conduct’ (it is in particular necessary to show that the function of, say, transferring funds or purchasing goods is one ‘which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments’). But the language of these two provisos – which are themselves guarding against the abuse of subparagraph (iv) – is extremely unclear. As noted elsewhere, to give meaning to this idea of ‘normal governmental conduct’ is far from easy.<sup>91</sup> To sum this up, ‘[t]he notion of *normality* is ... an uncertain criterion that may be interpreted in various ways’.<sup>92</sup>

To sum up, the use of a particularly demanding notion of ‘public body’ may lead to under-inclusion, ie a scenario where certain measures that should be covered by subsidy rules may in fact be left outside the scope of the disciplines. One truly wonders whether this result is in line with that the drafters intended.

*Canada – Certain Measures Affecting the Renewable Energy Generation Sector and Canada – Measures Relating to the Feed-in Tariff Program (Canada – Renewable Energy/FIT) (DS 412, 426)*

In the recent *Canada – Renewable Energy/FIT*, both the panel and the Appellate Body interpreted the requirement of a ‘benefit’. They called into question the established ‘market-orientation’ of the benefit test and, at the same time, injected the analysis of public policy objectives into the analysis of the benefit. The majority of the Panel controversially found that the various benchmarks put forward by the complainants could not be accepted.<sup>93</sup> This decision was justified by the fact that:

competitive wholesale electricity markets, although a theoretical possibility, will only rarely operate in a way that remunerates the mix of generators needed to secure a *reliable* electricity system with enough revenue to cover their all-in costs, let alone a system that pursues *human health and*

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<sup>91</sup> Luca Rubini, ‘Ain’t Wastin’ Time No More. Subsidies for Renewable Energy, the SCM Agreement, Policy Space, and Law Reform’, (2012) *J. of Intl Eco. L.*, p. 525. At pp. 541-544.

<sup>92</sup> Rubini, n. 91 above, at p. 543. ‘In a brief paragraph, the Appellate Body has recently shed some light on its reading of the two final sentences of subparagraph (iv) by referring to ‘*what would ordinarily be considered part of governmental practice in the legal order of the relevant Member*’ and ‘*within WTO Members generally*’ [Appellate Body, *US – AD/CVD*, WT/DS379), para. 297]. This apparently disposes of more abstract or philosophical approaches about what government is or should be in favour of a more factual one. Crucial issues remain open though. How does one define ‘ordinarily’? What is the relevant baseline? Is there a minimum recurrence or a certain pattern that makes something ‘ordinary’? Furthermore, moving to the interpretation of ‘practices normally followed by governments’, how do we define what ‘WTO Members generally’ do? Does this mean ‘what most governments do’? If so, is there a minimum number of governments that is required to satisfy the evidential burden? In our view, the open-ended nature of these questions shows the inherent flexibility of the concept of ‘normality’ that cannot rest on a simple examination of legal systems or on empirical surveys’. A qualitative judgment is eventually called for, one that is (more) prone to conclusions based (also) on policy preferences’.

<sup>93</sup> One Panelist dissented and concluded that the Canadian measure did confer a benefit and constitute a subsidy.

*environmental* objectives through the inclusion of facilities using solar PV and wind technologies into the supply mix.<sup>94</sup>

After defining the relevant product market as including renewable (i.e. wind and solar) energy only,<sup>95</sup> the Appellate Body introduced a distinction between government interventions that ‘create’ markets that would not otherwise exist and government interventions in support of certain players in already existing markets. While the former would not in and of itself be subject to subsidy law scrutiny, in particular *if* certain conditions of proportionality are satisfied, the latter would, by contrast, be fully subject to subsidy laws and market benchmarking.

Although the implications of these potentially far-reaching findings are not yet clear, there is broad agreement that they may offer a carve-out for many policies in support of renewable energy and even beyond this sector. The eventual outcome is that certain ‘subsidy’ measures are not covered by the ‘subsidy’ definition with possible serious systemic implications. It therefore comes as no surprise that these decisions have been strongly criticised in the literature.<sup>96</sup>

*Canada – Certain Measures Affecting the Renewable Energy Generation Sector and Canada – Measures Relating to the Feed-in Tariff Program (Canada – Renewable Energy/FIT) (DS 412, 426)*

In *US – Carbon Steel*, the Appellate Body interpreted the expression ‘a government practice involves a direct transfer of funds’, which is the first type of financial contribution under Article 1.1(a)(1) of the SCM Agreement.

The Appellate Body contrasted the adjective ‘direct’, which would indicate ‘something occurring immediately, without intermediaries or interference’,<sup>97</sup> with the word ‘involves’ which would suggest that the government action does not necessarily need to consist of a transfer of funds but ‘may be a broader set of conduct in which such a transfer is implicated or included’.<sup>98</sup> Even more explicitly the Appellate Body went on to say that ‘[t]he term also appears to introduce an element suggesting a lack of immediacy to the extent that it does not prescribe that a government must necessarily make the direct transfer of funds, but only that there be a “government practice” that “involves” the direct transfer of funds.’<sup>99</sup> This inevitably led to the

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<sup>94</sup> Panel Report, para. 7.309 (emphasis in the original). The dissenting Panelist opined that an appropriate benchmark could be found, even in a hypothetical competitive market, in the wholesale market that ‘could’ exist in Ontario. He was also quite adamant that public policy objectives should not interfere with the market analysis of the benefit test.

<sup>95</sup> This conclusion was based on a wrong application of market definition analysis, unwarrantedly borrowed from the antitrust toolbox.

<sup>96</sup> See, e.g., Aaron Cosbey and Petros C Mavroidis, ‘A Turquoise Mess: Green Subsidies, Blue Industrial Policy and Renewable Energy: the Case for Redrafting the Subsidies Agreement of the WTO’ (2014) *Journal of International Economic Law*, pp. 1-37; Charnovitz and Fischer, ‘Canada – Renewable Energy. Implications for WTO Law on Green and Not-So Green Subsidies’ (2015) *World Trade Review* 177-210; Luca Rubini, n. **Error! Bookmark not defined.** above. For a comprehensive literature review see Luca Rubini, ‘The Wide and the Narrow Gate. Benchmarking in the SCM Agreement after the *Canada – Renewable Energy/FIT Ruling*’ (2015) *World Trade Review* 211-237.

<sup>97</sup> Appellate Body Report, para. 4.89.

<sup>98</sup> Appellate Body Report, para. 4.90.

<sup>99</sup> Appellate Body Report, para. 4.90.

conclusion that this form of financial contribution might include a transfer effectuated through an intermediary.<sup>100</sup>

The Appellate Body then perceptively noted:

We also do not consider that the foregoing interpretation of the scope of Article 1.1(a)(1)(i) renders Article 1.1(a)(1)(iv) [which primarily regulated ‘indirect’ financial contributions] inutile. Depending on the nature of the involvement of an intermediary in the transfer of an alleged subsidy, the outcome may differ under subparagraph (i) and subparagraph (iv). For instance, there may be circumstances where the intermediary acts as “entrusted” or “directed” by the government. In yet other circumstances, the intermediary may not have been accorded sufficient entrustment or direction in order to effect the type of financial contribution contemplated under Article 1.1(a)(1)(iv), but may yet still qualify under Article 1.1(a)(1)(i).<sup>101</sup>

This passage is crucial to the interpretation of the definition of subsidy. One wonders whether the Appellate Body is ingeniously uncovering a difference that, to the best of our knowledge, nobody has ever noted before, and, in so doing, it is splitting hairs, or, in other words, is indulging in a unduly pedantic exercise of textual hermeneutics with exaggerated semantics that ends up betraying the object and purpose of the provision. Moreover, how can two arguably opposing forces embodied in the financial contribution – on the one hand, the requirements for ‘directness’, on the other that of ‘lack of immediacy’ – be operationally reconciled? How can scenarios under subparagraph (i) really be distinguished from those under subparagraph (iv)?

Indeed, the adopted interpretation carries two risks. The first concerns the ‘internal’ balance within the definition of subsidy, and the real danger of emptying the fourth subparagraph of Article 1.1(a)(1) of the SCM Agreement of its clear function (which is convincingly elucidated, also with reference to the negotiating history, in the *US – Export Restraints* Panel report commented above). The second affects the ‘external’ balance of the definition (i.e. that pertaining the scope of the notion of subsidy) and is similar to that of the arguably too broad prevailing construction of the terms ‘entrust’ and ‘direct’ after *US – DRAMs* as analysed above. In simple terms, the Appellate Body may have created new inroads into the scope of the disciplines in a manner that was not intended by those who negotiated and drafted them.

One final gloss which shows how one error may lead to another. At issue were two different bodies, i.e. the Steel Development Fund (SDF) and the Joint Plant Committee (JPC). The US DOC had imposed CVDs after concluding that the SDF, and in particular its Managing Committee, was a public body and that it had made all the decisions related to the loans at issue, whose disbursements were however administered by the JPC. Because the SDF Managing Committee made all the decisions regarding on the issuance of the loans the Panel concurred with the US DOC and accepted that the former was directly involved in their provision. It may well be that, had the notion of ‘public body’ still relied on governmental control (despite the Appellate Body’s dictum in *US – AD/CVD*), *all* relevant bodies in this case (i.e. both the SDF and the JPC) might easily have been considered to be public

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<sup>100</sup> Appellate Body Report, para. 4.94.

<sup>101</sup> Appellate Body Report, para. 4.95.

bodies, making the issue analysed in this section redundant and avoiding the need for the Appellate Body to step into dangerous territory.

## 7. Taking stock: initial observations

At this stage, it may be useful to group together the various decisions analyzed so far. As noted above, there are four types of decisions, according to the assessment given: correct decisions, those raising serious doubts, wrong decisions and finally seriously wrong decisions. The standard of assessment focuses on whether, and if so to what extent, the relevant adjudicating body has followed the negotiated balance of the provisions at issue (a more detailed analysis of this assessment follows in Section H). Table 11.2 offers a visual aid and also shows the decisions attributed to panels (P) or the Appellate Body (AB).

**Table 2** – Summary of assessment of reviewed decision

Correct decisions	Decisions raising serious doubts	Wrong decisions	Seriously wrong decisions
<i>Canada – Aircraft</i> (P, AB) <i>US – Export Restraints</i> (P) <i>US – FSC</i> (P, AB) <i>US – FSC (21.5)</i> (P, AB) <i>China – GOES</i> (P) <i>US – Lumber IV</i> (P) <i>US – DRAMS</i> (P) <i>Korea – Commercial Vessels</i> (P) <i>EC – DRAMS</i> (P) <i>US – AD/CVDs</i> (P) <i>US – Carbon Steel</i> (P)	<i>US – DRAMs</i> (AB) <i>US – AD/CVDs</i> (AB) <i>US – Carbon Steel</i> (AB)	<i>US – Lead Bars II</i> (P, AB) <i>US – CVDs on EC Products</i> (P, AB)	<i>US – Lumber IV</i> (AB) <i>Canada – Renewable Energy/FIT</i> (P, AB)

Very basic data analysis shows that, of 24 decisions, 14 have been assessed as correct, 7 wrong to a varying degree, and 3 as highly dubious. Of the 14 correct ones, the large majority (11) comes from Panels. This contrasts to the set of questionable decisions, of which 7 (out of 10) were adopted by the Appellate Body.

Assuming the sampling is meaningful and the assessment is correct, this seems to immediately indicate that panel decisions in the subsidy field are on the whole more likely to follow the negotiated balance of the law than those of the Appellate Body. This result is particularly significant because of the greater number of panel (14) vis-à-vis Appellate Body (10) decisions reviewed. That being said, we need a little more analysis before reaching a more definite conclusion.

## 8. Have the panels and Appellate Body searched for the ‘negotiated balance’?

It is now time to specifically apply the concepts of ‘negotiated balance’ and ‘point of balance’ to the samples of good and bad cases analysed above. Have the relevant panels and the Appellate Body made use of these concepts and, if so, to what extent? In other words, have they referred to what the drafters meant (by looking at what they said in the negotiating documents) or must have meant, or not have meant (by logical

implication)? If not, to what extent did their reasoning differ from the negotiated balance?

In the cases exemplifying what I call ‘jurisprudence of discovery’ there is good evidence that the relevant panels and Appellate Body paid considerable attention to detecting the ‘negotiated balance’ or the ‘balance point’ of the relevant provisions and disciplines. For example, in *Canada – Aircraft* they did so by considering the objective of the agreement, which, however vague, was identified in the need to control trade-distorting subsidies, and then directly making a connection between that objective and the use of the marketplace as the inevitable benchmark. It is only by reviewing what happens - or would happen - in the market as it exists when the government intervenes that one can identify the trade-distorting potential of the action of the government,<sup>102</sup> which is what ultimately matters in WTO subsidy disciplines. In *US – FSC* they struggled to identify a clear logical expression for the test required by the ‘otherwise due’ language. However, they rightly found this to be a formal test, largely based on whether the US measures at issue were derogating (or otherwise) from the conduct previously established by the same US. In so doing, they implicitly rejected the possibility of *defining* subsidies by taking into account their broader political and economic objectives or effects, such as the need to equalise or compensate for the impact of other competing tax systems. This is – in our view – part and parcel of the inherent logic of the SCM Agreement. Finally, in *US – Export Restraints* and, by reference, in *China – GOES*, the two Panels expressly sought illumination from the negotiating history. In so doing, they avoided that the parties reopened hard-fought agreements and respected the delicate balance that the compromised definition of Article SCM 1 enshrines.

By contrast, in the cases belonging to the ‘jurisprudence of invention’ the Appellate Body and panels go against the balance and logic of the SCM Agreement, of the relevant provision or even of the legal requirement at issue. In some cases, this happens because, by not being economically informed in highlighting what matters in the benefit analysis (i.e. do we still have a distortion in the market?), they go against the general objective of the SCM Agreement (see *US – Lead Bars II* and *EC – CVDs on EC Products*). The same outcome is evident in the *Canada – Renewable Energy/FIT* dispute, where both the Panel and the Appellate Body intentionally inject public policy considerations into the benefit determination, and thus clearly depart from the conception of benefit and subsidy that the negotiators had in mind. In *US – Lumber IV* this is taken in an even more dramatic direction. The Appellate Body goes against the clear letter of the law and substitutes themselves for the drafters. Finally, in other decisions, the Appellate Body (not the panels) takes adventurous paths and produces novel interpretations that, by expanding or reducing the meaning of certain legal requirements, seriously risk unsettling the balance of the definition and hence of the disciplines themselves (see *US – DRAMS*; *US – AD/CVD*; *US – Carbon Steel (India)*).

The analysis seems to confirm that, at least in the context of subsidy jurisprudence, panels have on the whole been more self-restrained (and correct).<sup>103</sup>

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<sup>102</sup> Appellate Body Report, para. 157.

<sup>103</sup> One good explanation may be that the panels adhere more closely to the text and the intention of the drafters because, at least until 2008, they had - through the Secretariat - access to Jan Woznowski. By having closely assisted the Chair during the Uruguay Round negotiations, he was familiar with the



## 9. The age of innocence

Recently, on the occasion of a luncheon address at a conference marking the twentieth anniversary of the WTO Appellate Body,<sup>106</sup> Professor Joseph Weiler emphatically argued that the ‘first’ WTO jurisprudence was characterized by some sort of infancy or immaturity and showed lack of self-confidence by continuing to refer to the negotiating history of the relevant WTO provisions. Then – so the argument went – came the age of maturity and the adjudicators were finally liberated from this burden and able to walk on their own two feet.<sup>107</sup> For the reasons expressed in this brief paper, I do not agree with this interpretation.

The reference and reliance on the justification of the law, which in the contractual context of the WTO goes back to its roots and origins in the negotiations, is not a symptom of lack of experience or self-confidence, nor of subscribing to any (neo-liberal) agenda, but rather a sign of maturity of the court. This, of course, cannot be stated in general terms for any legal system and any court. But – we believe – it is certainly valid in the context of a political and legal system such as the WTO and with respect to its uniquely successful dispute settlement system.

On the occasion of its twentieth anniversary, recent scholarship has concentrated on general assessments of WTO dispute settlement.<sup>108</sup> This is often looked at through the lens of the notion of legitimacy. This is not limited to offering learned narratives about the Appellate Body’s contribution to the building of WTO law through its case-law,<sup>109</sup> but extends to its assessment through empirical evidence. In particular, interviews with key WTO practitioners would thus show how the WTO adjudicating bodies, and in particular the Appellate Body, can be said to have succeeded in using various jurisprudential, procedural and rhetorical device to specifically respond to the demands of their different audiences.<sup>110</sup>

Be it as it may, in this paper I have presented a different narrative of the case-law, and suggested a different approach to the interpretation of the WTO covered agreements, using subsidy jurisprudence as case-study. To put it another way, this paper has an important normative – not sociological – point to make. There are various meanings of legitimacy<sup>111</sup> but, ultimately, I believe that adjudicators, and in

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<sup>106</sup> The ‘WTO Appellate Body @ 20: Taking Stock and Looking Forward’, 15<sup>th</sup> May 2015, European University Institute, Florence.

<sup>107</sup> Rob Howse has recently provided a new interpretation of the Appellate Body’s disengagement from the negotiating history, which would put the WTO era in stark contrast to the GATT period. The effective downgrading of negotiating history (and even the express reliance on Article 32 of the VCLT, which frames the latter within the ‘supplementary means of interpretation’) would represent an intentional device to gain independence from the WTO ‘institution’ and its political-diplomatic trade circle. See Howse, n. 105 above, p. 32.

<sup>108</sup> See, e.g. Petros Mavroidis, *Dispute Settlement in the WTO: Mind over Matter* (2016).

<sup>109</sup> The best example in point is Howse, n. 105 above, pp. 9-77.

<sup>110</sup> See Sivan Shlomo-Agon, ‘Clearing the Smoke: The Legitimation of Judicial Power at the WTO’ (2015) *Journal of World Trade*, pp. 539-590.

<sup>111</sup> Weiler juxtaposes a ‘sociological’ approach to legitimacy and a ‘normative’ one. See Joseph Weiler, ‘Epilogue: Judging the Judges – Apology and Critique’ in Maurice Adams, Henri de Waele, Johan Meeusen and Gert Straetmans (eds), *Judging Europe’s Judges – The Legitimacy of the Case Law of the European Court of Justice* (Oxford and Portland, Oregon: Hart Publishing, 2013), 235.



particular those acting in the specific political and legal context of the WTO, *should* pay attention to the legitimacy that inevitably flows from the legality of their decisions and reasoning. And the legality of judicial decisions must be measured against their formal correctness. Key to this, as this paper has argued, is the WTO judges' effort to rely on what the negotiators have agreed to - no more no less.

At twenty, the age of innocence is definitely over. At the time of writing, very dark clouds are gathering over the Appellate Body - and the WTO at large.<sup>112</sup> It would be extremely unfortunate if these events, determined by political forces, would undermine the success story of the WTO dispute settlement system. If external, and largely illogical, events cannot be controlled, the WTO dispute settlement system can, however, certainly reflect on its story, weigh up its success, carefully consider its crucial and delicate role in the WTO system, and, in the most crucial step, it must measure up to it.

Contact:

Luca Rubini  
School of Law  
University of Birmingham  
Edgbaston  
B15 2TT Birmingham UK  
e-mail: l.rubini@bham.ac.uk

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<sup>112</sup> The US have announced that they will block the reappointment of one member of the Appellate Body (Seung Wha Chang) essentially because he did participate in decisions against the US. See Greg Shaffer, *Will the US Undermine the World Trade Organization?*, *The World Post*, 23<sup>rd</sup> May 2016.