WTO CASE REVIEW 2007[#]

Raj Bhala[*] & David Gantz[**]

#. This *WTO Case Review* is the eighth in our annual series on the substantive international trade adjudications issued by the Appellate Body of the World Trade Organization. Each *Review* explains and comments on the Appellate Body reports adopted by the WTO Dispute Settlement Body during the preceding calendar year (Jan. 1 – Dec. 31), excluding decisions on compliance with recommendations contained in previously adopted reports. *See* Raj Bhala & David Gantz, *WTO Case Review 2006*, 24 ARIZ. J. INT'L & COMP. L. 299 (2007); Raj Bhala & David Gantz, *WTO Case Review 2005*, 23 ARIZ. J. INT'L & COMP. L. 107 (2006); Raj Bhala & David Gantz, *WTO Case Review 2004*, 22 ARIZ. J. INT'L & COMP. L. 99 (2005); Raj Bhala & David Gantz, *WTO Case Review 2003*, 21 ARIZ. J. INT'L & COMP. L. 317 (2004); Raj Bhala & David Gantz, *WTO Case Review 2002*, 20 ARIZ. J. INT'L & COMP. L. 143 (2003); Raj Bhala & David Gantz, *WTO Case Review 2001*, 19 ARIZ. J. INT'L & COMP. L. 457 (2002); Raj Bhala & David Gantz, *WTO Case Review 2000*, 18 ARIZ. J. INT'L & COMP. L. 1 (2001).

We are grateful to the Editors and Staff of the *Arizona Journal of International and Comparative Law* for their excellent editorial assistance and continuing support of our work.

The WTO reports we discuss are available on the web site of the WTO, at http://www.wto.org/english/tratop_e/dispu_e/find_dispu_cases_e.htm. The texts of the WTO agreements we discuss are also available on the WTO web site (http://www.wto.org/english/docs_e/legal_e/legal_e.htm) and are published in a variety of sources, including Raj Bhala, *International Trade Law Handbook* (3rd ed. 2008). We endeavor to minimize footnotes and, toward that end, provide citations to indicate sources from which various portions of our discussion are drawn.

*. Rice Distinguished Professor, The University of Kansas, School of Law, Green Hall, 1535 West 15th Street, Lawrence, KS 66045-7577 U.S.A. Tel. 785-864-9224. Fax. 785-864-5054. www.law.ku.edu. Author of the treatise *Modern GATT Law* (Sweet & Maxwell 2005) and the textbook *International Trade Law: Interdisciplinary Theory and Practice* (3d ed., LexisNexis, 2008). Professor Bhala is grateful to his Research Assistant, Mr. Ben Sharp (B.S., Kansas State University, 2003; M.Sc., London School of Economics, 2005; J.D. Class of 2009, University of Kansas), for his indispensable help on this work.

**. Samuel M. Fegtly Professor of Law; Director, International Trade Law Program; Associate Director, National Law Center for Inter-American Free Trade, University of Arizona, James E. Rogers College of Law; Associate Director, National Law Center for Inter-American Free Trade. Tel. 520-621-1801. Fax. 520-621-9140. www.law.arizona.edu.

Table of Contents **Page**

PART I: INTRODUCTION

Except for major changes in the composition of the Appellate Body, it was a relatively quiet year, with a record low number of new appeals. The numbers, however, conceal evidence of significant challenges coming to the system in 2008, including those related to government subsidies of Boeing and Airbus, China's alleged failure to implement its WTO obligations, Europe's restrictions on genetically modified organisms, and on-going implementation disputes over U.S. agricultural subsidies and prohibitions on Internet gambling.[1]

Also, as it becomes increasingly clear that the Doha Development Round of WTO negotiations will not be completed in 2008, or perhaps even 2009,[2] the number of new requests for

---

1. *See, e.g.*, Request for Consultations by the United States, *China — Measures Affecting the Protection and Enforcement of Intellectual Property Rights*, WT/DS362/1 (Apr. 16, 2007); Request for Consultations by Canada, *United States — Subsidies and Other Domestic Support for Corn and Other Agricultural Products*, WT/DS357 (Jan. 8, 2007); Request for Consultations by the United States, *European Communities — Measures Affecting Trade in Large Civil Aircraft* (Second Complaint), WT/DS347 (Jan. 31, 2006); Request for Consultations by the European Communities, *United States — Measures Affecting Trade in Large Civil Aircraft* (Second Complaint), WT/DS353 (June 27, 2005); Request for Consultations by the United States, Canada & Argentina, *European Communities — Measures Affecting the Approval and Marketing of Biotech Products*, DS291, 292, 293 (May 2003). WTO, Chronological List of Dispute Cases, http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm.

2. A detailed discussion of the reasons for the stalemate in the negotiations is beyond the scope of this article. In addition to the two year old standoff between developed and developing countries over agricultural subsidies, agricultural market access, and non-agricultural market access, the prospects of completing the negotiations are complicated by current political considerations. For example, in the European Union, a new legal structure based on the Treaty of Lisbon, Dec. 13, 2007, 50 O.J. C306, *available at* http://eur-lex.europa.eu/JOHtml.do?uri=OJ:C:2007:306:SOM:EN:HTML (last visited Dec. 18, 2007) is to be implemented in 2008, suggesting a continuing focus on internal matters after an expansion of the EU to 27 Members in 2007. In the United States, the U.S. presidential election, the expiration of the president's "Trade Promotion Authority" on June 30, 2007, and a slowing U.S. economy all make the prospects of a breakthrough in Geneva even less likely than in 2007. *See, e.g.*, *Economics and Politics in 2008 Dampen Hopes for Conclusion to Doha Round,* 25 INT'L TRADE REP. (BNA) 90 (2008) (discussing the U.S. political factors that make agreement in Geneva unlikely in the near term). Some believe that India, China, and Brazil, among other developing nations, will continue to thrive despite a downturn in the U.S. economy and

consultations may well increase as Members become resigned to the fact that the current WTO rules (including those relating to agricultural subsidies and dumping, and to revision of the Dispute Settlement Understanding ("DSU")[3]) are likely to remain in force, unchanged, for at least several more years.

I. FOUR NEW FACES ON THE APPELLATE BODY

In an unusual process, the Dispute Settlement Body ("DSB") filled four immediate and impending vacancies on the Appellate Body (out of seven members) in a series of interviews and related proceedings concluded on November 27, 2007. Normal practice in the Appellate Body is for the members to serve initial four-year terms with one reappointment, as provided in the DSU.[4] However, this is not a hard and fast rule; Professor Merit Janow's decision to retire in December 2007 recalls the decisions of Said El-Naggar and Professor Mitsuo Matsushita not to stand for reappointment in 2000.[5] In the course of the selection process, the DSB selected Lilia Bautista (Philippines) and Jennifer Hillman (United States) to serve four year terms beginning December 11, 2007, and Shotaro Oshima (Japan) and

---

thus remain uninterested in making the necessary Doha compromises. Others, including the authors, are more skeptical.

3. Little progress has been made recently in the "Special Session of the Dispute Settlement Body," the group charged with conducting negotiations relating to the DSU under Doha. In December 2007, the chair of the Special Session reported that since May "the work of the DSB Special Session has continued to be based primarily on efforts by Members working among themselves . . . ." He also indicated that he had been consulting with Members concerning various Member proposals and that a joint proposal of Cuba, Egypt, Malaysia, and Pakistan on special and differential treatment (for developing Members) along with a revised proposal anticipated from the African Group, would be addressed in upcoming consultations in early 2008. Special Session of the Dispute Settlement Body, *Report by the Chairman, Ambassador Ronald Saborio Soto, to the Special Session of the General Council*, TN/DS/21 (Dec. 6, 2007), *available at* http://docsonline.wto .org/DDFDocuments/t/tn/ds/21.doc (last visited Feb. 6, 2008).

4. Understanding on Rules and Procedures Governing the Settlement of Disputes, art. 4.1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, Legal Instruments – Results of the Uruguay Round, 33 I.L.M. 1125 (1994) [hereinafter DSU]

5. Appellate Body, *Annual Report for 2007*, Annex 2, WT/AB/9 (Jan. 30, 2008), *available at* http://www.wto.org/english/tratop_e/dispu_e/ab_annual_report07_e.doc [hereinafter Annual Report].

Yuejiao Zhang (China) to serve four-year terms beginning June 1, 2008.[6]

As of June 1, 2008, the Appellate Body will have only three members who have served more than six months, a situation faced only once before, at the outset in 1995. It would not be practical (or consistent with the Working Procedures) for the DSB to ensure that at least one more experienced member sits on each division of three hearing a particular appeal, since the Working Procedures provide in pertinent part that "[t]he Members constituting a division shall be selected on the basis of rotation, while taking into account the principles of random selection, unpredictability and opportunity for all Members to serve regardless of their national origin."[7] Even if it were otherwise permitted to depart from the customary practice of choosing divisions, changing the rotation practice could raise concerns, particularly among the newer members of the Appellate Body. Fortunately, under the Working Procedures, the entire Appellate Body effectively participates in each proceeding: "[T]he division responsible for deciding each appeal shall exchange views with the other Members before the division finalizes the appellate report for circulation to the WTO Members."[8] Also, the WTO Appellate Body Secretariat remains under the direction of Werner Zdouc, who has served in the WTO's Legal Affairs Division since 1995 and as director of the Appellate Body Secretariat since 2006.[9]

II. WORK OF THE APPELLATE BODY

Only two appeals were filed in original proceedings in 2007, the lowest number since the creation of the DSB[10] in 1995.[11] In the

---

6. *Id.* at 4-5; *see* WTO Press Release, WTO Appoints Four New Appellate Body Members, Nov. 27, 2007, *available at* http://www.wto.org/english/news_e/pres07_e/pr501_e.htm (last visited Nov. 28, 2007) (discussing the appointment process).

7. Working Procedures for Appellate Review, Rule 6(2), Jan. 4, 2005, *available at* http://www.wto.org/english/tratop_e/dispu_e/ab_e.htm (last visited Feb. 6, 2008).

8. *Id.* at Rule 4(3).

9. Annual Report, *supra* note 5, at 27.

10. DSU, *supra* note 4, at art. 2.

11. Annual Report, *supra* note 5, at 30. No appeals were filed in 1995; under the DSU, art. 20, panel procedures are to be completed within nine months of the date the panel was established, or twelve months if the panel report is appealed. Since panels are not formed until 60 days after a mandatory request for consultations (art. 4:7), and a Member can delay the formation of

twelve years during which the Appellate Body has operated (again excluding 1995), appeals in original proceedings (72 in all) have varied from a high of eleven in 2000 to the low in 2007, for an average of six per year.[12] The frequency of appeals in new Article 21.5 proceedings[13] has ranged from a high of four in 2001 to a low of zero in 2004; there were two in 2007, and such appeals have averaged 1.75 per active year.[14]

The percentage of panel reports appealed to the Appellate Body has declined gradually over time, from 100% in 1996 and 1997, to only 50% in 2007, for an average of 67%.[15] There are a number of likely reasons for this. First, some of the cases now decided by panels involve questions that have already been resolved by the Appellate Body, and it is anticipated that the Appellate Body would take a similar approach in subsequent cases, as is normally the situation. Second, Members appear to have become more sophisticated in their use of the Appellate Body. Members no longer universally assume that exhaustion of all available judicial remedies is in the national interest or essential to defending a loss before the DSB at home. Third, appealing creates a risk that the Appellate Body will affirm a panel decision considered questionable by the losing Member, giving that ruling greater weight because it emanates from the Appellate Body rather than simply from a panel.

For example, the United States elected in advance not to appeal in *United States – Shrimp Antidumping.*[16] This decision was part of an understanding in which the United States and Ecuador agreed on an expedited procedure for a panel review of Ecuador's contention that the United States had applied its "zeroing" methodology in anti-dumping actions in a manner inconsistent with Article 2.4.2 of the *Antidumping Agreement,*[17] as determined by the Appellate Body in an

---

the panel for at least thirty days after the consultation period (art. 6:1), there could not have been any ripe appeals in 1995, even if a request for consultations had been filed in early January.

12. *Id.*

13. Disputes over whether steps taken to comply with the recommendations of the DSB were consistent with the requirements of the WTO Agreement in contention. DSU, *supra* note 4, at art. 21.5.

14. Annual Report, *supra* note 5, at 30. The first art. 21.5 appeal was not filed until 2000, so the calculations are based on eight years of such appeals.

15. *Id.* at 31.

16 Panel Report, *United States – Antidumping Measure on Shrimp from Ecuador,* WT/DS335/R (adopted Feb. 20, 2007) [hereinafter US-Shrimp Antidumping].

17. Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement

earlier decision.[18] The United States had agreed that it would not contest the Article 2.4.2 claim, that it would consent to limit briefings and hearings to a minimum, and that it would comply within a "reasonable time" of six months.[19] Implicitly, therefore, the United States also agreed not to appeal, which was probably a very wise choice given the unlikelihood that the Appellate Body would have changed its often-stated views on zeroing.[20]

No direct correlation appears to exist between the number of appeals and the number of new cases filed, even if one accounts for the customary sixteen to eighteen month lag time between initial filing of the request for consultation and filing the appeal. WTO records show that 369 requests for consultation had been filed from January 1, 1995 through the end of 2007. These had resulted in 107 adopted panel and Appellate Body Reports, sixty mutually agreed situations, and thirty-one "other settled or inactive disputes."[21] While only thirteen requests for consultation were submitted in 2007, well below the recent peak of thirty-seven in 2002, wide year-to-year fluctuations are common: there were twenty requests for consultations in 2006, twelve in 2005 and nineteen in 2004.[22] (The effective data totals are difficult to assess accurately because often several case numbers are assigned to requests by different Members for consultations on the same measures.)

Twenty-eight panels, including those convened under DSU Article 21.5, were active as of the end of January 2008.[23] Obviously, if panel reports in a significant number of those are circulated during the first half of 2008, the Appellate Body could have a busy year even if only 50% or so of the panel reports are appealed.[24]

Establishing the World Trade Organization, Annex 1A, 1868 U.N.T.S. 201, *available at* http://www.wto.org/english/docs_e/legal_e/19-adp.doc [hereinafter Antidumping Agreement].

18. Appellate Body Report, *United States – Final Dumping Determination on Softwood Lumber from Canada,* WT/DS264/AB/R (adopted Aug. 31, 2004).

19. *US – Shrimp Antidumping, supra* note 16, at Attachment 2.

20. *See United States – Measures Related to Zeroing and Sunset Reviews,* discussed *infra* in the WTO Case Review.

21. Update of WTO Dispute Settlement Cases, Jan. 22, 2008, at i-ii, *available at* http://docsonline.wto.org/DDFDocuments/t/WT/DS/OV32.doc.

22. *Id.*

23. *Id.*

24. As of late January 2008, only two unadopted panel reports had been circulated, and as of early February, no appeals had been lodged. WTO, *Chronological List of Disputes Cases, available at* http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm.

PART II: DISCUSSION OF THE 2007 CASE LAW FROM THE APPELLATE BODY

I. GATT OBLIGATIONS

A. Exceptions

1. Citation

Brazil – Measures Affecting Imports of Retreaded Tyres, WT/DS332/AB/R (issued on 3 December 2007, adopted by the DSB on 17 December 2007) (complaint by the European Communities, with Argentina, Australia, China, Cuba, Guatemala, Japan, Korea, Mexico, Paraguay, Taiwan, Thailand, and the United States as Third Parties).[25]

2. Facts[26]

The *Brazil Tires* case is the first dispute in which a developed country has challenged an environmental measure of a developing country. The facts of the case, but not the entirety of the holdings and rationale, are straightforward. Brazil imposed strikingly discriminatory measures against imports of retreaded tires: an import ban, coupled with an anti-circumvention fine for violating the ban. The discrimination adversely affected exports of this merchandise from the European Communities (EC). The EC sued, and argumentation followed upon reasonably predictable lines. The Panel found that the controversial Brazilian measures were provisionally justified under GATT Article XX(b). However, the Panel ruled in favor of the EC

---

25. Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres*, WT/DS332/AB/R (Dec. 3, 2007) (complaint by the European Communities, with Argentina, Australia, China, Cuba, Guatemala, Japan, Korea, Mexico, Paraguay, Taiwan, Thailand, and the United States as third parties) [hereinafter *Brazil Tires* Appellate Body Report].

The Panel Report in the case is *Brazil – Measures Affecting Imports of Retreated Tyres*, WT/DS322/R (June 12, 2007) (complaint by the European Communities, with Argentina, Australia, China, Cuba, Guatemala, Japan, Korea, Mexico, Paraguay, Taiwan, Thailand, and the United States as third parties)[hereinafter, *Brazil Tires* Panel Report].

26. This discussion is drawn from *Brazil Tires* Appellate Body Report, *supra* note 25, ¶¶ 1-8, 118-132; *Brazil Tires* Panel Report, *supra* note 25, §§ I-II.

because the measures did not satisfy the *chapeau* to that Article, a narrow ground based on Brazilian court injunctions that permitted imports of used tires. The EC appealed, and successfully persuaded the Appellate Body to broaden the basis of the ruling against Brazil, particularly under the *chapeau*.

a. What are Retreaded Tires?

Retreaded tires are produced by reconditioning used tires. The reconditioning process involves stripping the worn tread from the skeleton (also called the "casing") of a used tire, and replacing that worn tread with a new tread. On some used tires, part or all of the sidewalls are replaced, too. There are three basic retreading processes: (1) top-capping, in which only the tread is replaced; (2) re-capping, in which the tread and part of the sidewall are replaced; and (3) re-moulding (also called the "bead to bead method"), in which the tread and sidewall (*i.e.*, essentially the entire lower area of a tire) are replaced.

For purposes of customs classification, retreaded tires fall under heading 4012 of the Harmonized System (HS), which bears the description "Retreaded or used pneumatic tyres of rubber; solid or cushion tyres, tyre treads and tyre flaps, of rubber." Retreaded tires are distinguished from new tires, which are classified in HS heading 4011 and from used tires, which are slotted in HS sub-heading 4012.20. Within the retreaded tires heading, there are four sub-headings that distinguish such tires by use: (1) retreaded tires for motor cars (HS 4012.11); (2) retreaded tires for buses or lorries (HS 4012.12); (3) retreaded tires for aircraft (HS 4012.13); and (4) all other retreaded tires (HS 4012.19).

b. Risks from Retreaded Tires

Americans and other car consumers in developed countries are familiar with seeing new tires on new cars. However, in poor countries, use of retreaded tires on new cars – or, at least, the choice of having new or retreaded tires – is more common. On average, a tire – whether new or retreaded – can be used on a car for five years before it is considered "used." At the end of its useful life, a tire becomes "waste," unless, of course, the tire can be retreaded. The *Brazil Tires* case did not involve any claim that retreaded tires on vehicles are less safe than new tires (the lifespan of retreaded tires tends to be shorter than that of

new tires, so they generally reach the stage of "waste" earlier). International safety standards exist as to retreaded tires; passenger car tires may only be retreaded once. Rather, this case concerned whether the environmental impacts of retreaded tires justified Brazil's trade measures.

What are those impacts? Generally, there are two broad categories of risks to human life and health from the accumulation of waste tires, including:

- Transmission of dengue fever, malaria, and yellow fever through mosquitoes, which use discarded tires as a breeding ground.

- Exposure to toxic emissions caused by tire fires. Such emissions can cause cancer, cardiovascular ailments, immune system suppression, learning disabilities, premature mortality, reduced lung function and other respiratory and chest problems, and short-term memory loss.

Waste tires also pose to plants and animals the same risks of mosquito-borne disease and exposure to toxic emissions.

Significantly, then, governments are wont to minimize the adverse effects of waste tires. Some of them have taken preventive steps to decrease the number of waste tires generated. Others have adopted remedial measures to dispose of waste tires, such as proper incineration, landfilling, recycling, and stockpiling. Still another policy tool is an import ban. Brazil is not the only country to ban imports of retreaded tires. Argentina, Bangladesh, Bahrain, Morocco, Nigeria, Pakistan, Thailand, Tunisia, and Venezuela are among the countries restricting importation of retreaded or used tires.

c. Brazil's Controversial Measures

Brazil implemented five categories of measures affecting international trade in retreaded tires:

- An import ban on retreaded tires, effected on November 17, 2004 by the Secretariat of Foreign Trade of the Ministry of Development, Industry and Foreign Trade (SECEX), via Article 40 of Portaria

No. 14 ("Portaria SECEX 14/2004").[27] The Article 40 "Import Ban" forbids issuance of import licenses for retreaded tires.[28]

- A set of rules and regulations, dating between January 7, 1998 and November 28, 2004, banned the importation of used tires; the Brazilian government sporadically applied these regulations.[29] The rules and regulations were issued by various governmental authorities – the Department of Foreign Trade Operations (DECEX), the Brazilian Institute of the Environment and of Renewable Resources (IBAMA), the National Council for the Environment of the Ministry of the Environment (CONAMA), the Ministry of Industry, Commerce, and Tourism, and the Ministry of the Economy. Some rules and regulations concerned collection and disposal schemes for waste tires. For example, a CONAMA regulation dating from 1999, and amended in 2002, established environmentally appropriate disposal obligations. However, the regulation exempted domestic tire retreaders from those obligations, as long as they processed tires consumed in Brazil. That is, the regulation encouraged Brazilian retreaders to retread domestically used tires.

- A Presidential Decree of September 14, 2001 imposing a fine of 400 Brazilian real (BRL) per unit on the importation of retreaded tires. This anti-circumvention fine also applied to marketing, transporting, storing, keeping, or warehousing imported (but not domestic) retreaded tires.

- Rules in various Brazilian states prohibiting the sale of imported retreaded tires. One example is the state of Rio Grande do Sul. Its law of July 5, 2004 forbade commercialization of imported used or retreaded tires, or retreaded tires made in Brazil from

---

27. *See Brazil Tires* Appellate Body Report, *supra* note 25, ¶¶ 122-23 and accompanying footnotes.

28. Article 40 also precludes importation of used tires, but the EC did not challenge the prohibition on importation of used tires. *See id.* ¶ 123.

29. *Id.* ¶¶ 122, 128-31.

> imported casings. It amended that law on November 28, 2005 to allow importation and marketing of retreaded tires, but only if the importer destroys ten used tires in Brazil for every retreaded tire it imports (or destroys one used tire per imported used tire casing).
>
> • An exemption for remoulded tires imported from another MERCOSUR country from both the Portaria SECEX 14/2004 Import Ban and the Presidential Decree of September 14, 2001. This "MERCOSUR Exemption" was effected via a new rule of SECEX dated March 8, 2002, and through another Presidential Decree, dated February 11, 2003, and ultimately incorporated into Article 40 of Portaria SECEX 14/2004. The MERCOSUR Exemption eliminated the Import Ban on remoulded (but not other retreaded) tires originating in Argentina, Paraguay, and Uruguay. It was Brazil's direct response to a ruling of a MERCOSUR arbitral panel that had been established following a request from Uruguay on August 27, 2001. The MERCOSUR panel decided, on January 9, 2002, that the Import Ban violated MERCOSUR Decision CMC No. 22 of June 29, 2000, which enjoins MERCOSUR partners not to introduce new restrictions to commerce among each other.[30]

Not surprisingly given these measures, the EC at the WTO Panel stage argued that Brazil had violated GATT Articles I:1, III:4, XI:1, and XIII:1: the most-favored nation (MFN) rule, the national treatment rule for non-fiscal measures, the rule against quantitative restrictions (QRs), and the rule concerning administration of permissible QRs, respectively.[31]

Specifically, the EC alleged the Import Ban violated GATT Article XI:1, and could not be justified under Article XX. The MERCOSUR Exemption, the EC argued, violated Articles I:1 and XIII:1, and could not be justified by Article XXIV:5, or by the 1979 Tokyo Round *Enabling Clause*. Brazil did not contest that its Import Ban on retreaded tires was *prima facie* inconsistent with Article XI:1 or

30. *Id.* ¶ 122 n.163.
31. *Id.* ¶ 2.

that similar state measures were *prima facie* violations of Article III:4. Brazil also conceded that the exemption to its Import Ban and the fine for MERCOSUR parties were *prima facie* inconsistent with Articles I:1 and XIII:1.

Brazil defended any discrimination under GATT Article XX(b), namely, the Import Ban, anti-circumvention fines, and complementary state measures, as necessary to protect human, animal, and plant life and health. Brazil also advanced the Article XX(d) administrative necessity exception as a defense. It contended that the fines connected with the import prohibition on retreaded tires were administratively necessary to secure compliance with the Import Ban, which itself is not inconsistent with GATT. Likewise, the adjudicatory analysis was predictable, namely, application of the two-step test for any GATT Article XX defense: (1) does the measure in dispute fall within at least one of the ten exceptions itemized in Article XX and thereby become provisionally justified, and (2) if so, does the provisionally justified measure meet the requirements of the *chapeau* to Article XX?[32]

Rather unusual, but not unprecedented in WTO jurisprudence, was Brazil's defense that the limited derogation from its Import Ban for MERCOSUR countries—that is, the discrimination in favor of them—was authorized by GATT Article XXIV. Brazil made this defense in the context of the exemption from the import ban and associated fines on imports concerning remoulded tires—not all retreaded tires. Brazil reasoned that MERCOSUR was a customs union under Article XXIV, and the exemption permitting retreaded tire imports from MERCOSUR was consistent with that Article. Brazil also argued that the exemption from the ban and fines for remoulded tires was justified under GATT Article XX(d) as administratively necessary for Brazil to secure

---

32. *See Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 139. This test, developed by the Appellate Body through a series of precedents, is laid out in a variety of sources, including Raj Bhala, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE ch. 43 (3d ed. 2008).

The *chapeau* to Article XX states:

> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures.

See Raj Bhala, DOCUMENTS SUPPLEMENT TO INTERNATIONAL TRADE LAW doc. 3 (3d ed. 2008).

compliance with its MERCOSUR obligation, which itself is not inconsistent with GATT.

3. Panel Holdings and Appellate Issues

The conclusions and rationale were, like the facts, reasonably simple. First, the Panel held that Brazil's Import Ban on retreaded tires violated GATT Article XI:1 and could not be justified under Article XX. The Panel agreed that the Ban met Step One of the Two Step Test; the Ban was provisionally justified under Article XX(b) as "necessary to protect human, animal, or plant life or health." But, the Ban flunked Step Two, the *chapeau* of Article XX. The Panel found that importing used tires under Brazilian court injunctions constituted an application of the Import Ban that was, under the *chapeau*, (1) "a means of unjustifiable discrimination [between countries] where the same conditions prevail," and (2) "a disguised restriction on international trade."[33] Second, the Panel held that the fines that Brazil imposed for violating the Import Ban were illegal under Article XI:1 and could not be justified under either Article XX(b) or (d). Third, the Panel held that the Brazilian state law measures ran afoul of Article III:4 and could not be defended successfully under Article XX(b).

In sum, the EC's victory was nearly complete at the Panel stage. However, Brazil did receive two consolations. First, its loss was as narrow as possible. The Panel held that the MERCOSUR Exemption did not result in an application of the Import Ban that was inconsistent with the *chapeau* of GATT Article XX. Rather, the Panel based its finding on used tire imports under court injunctions. Significantly, it was primarily this aspect of the Panel Report—the narrow basis for the finding—that prompted the EC to appeal. The appeal also was prompted by doubts about the Panel's rationale as to the necessity of the Import Ban under GATT Article XX(b). More specifically, the EC questioned whether the Panel (1) used an erroneous legal standard in assessing the contribution of the Import Ban to the ends pursued by it, (2) correctly considered alternatives to the Import Ban, and (3) appropriately balanced relevant factors.

Brazil's second consolation was that the Panel exercised judicial economy on the rest of the EC claims; the Panel did not find that the MERCOSUR Exemption from the Import Ban and fines was unlawful under Articles I:1 and XIII:1. The Panel saw no need to

---

33. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 5 (parenthetical inserted by the Appellate Body).

adjudicate these claims, since it had found the Brazilian retreaded tire regime legally wanting on other grounds. The Panel's exercise of judicial economy on Brazil's justifications to those claims under Articles XX(d) and XXIV meant that Brazil was spared a truly sweeping defeat. Of course, it also meant that the international trade community did not get what might have been an important and intriguing decision on the relationship between GATT–WTO obligations and those of regional trade agreements (RTAs). The Appellate Body upheld the Panel's decision here and neither considered the Article I:1 or XIII:1 claim nor defenses to them under Articles XX(d) and XXIV.[34]

On appeal, the anti-circumvention fines were not at issue.[35] Likewise, neither rules and regulations of various Brazilian governmental bodies nor state laws—such as those of Rio Grande do Sul—were at issue at the appellate stage.[36] Also not at issue were Brazilian court injunctions allowing Brazilian retreaders to import used tire casings so that they could manufacture retreaded tires from those casings.[37] Rather, the appeal focused on two issues:[38] the necessity of the Import Ban under GATT Article XX(b),[39] and the application of the *chapeau* of Article XX to the Ban.[40]

---

34. *Id.* ¶¶ 117(c), 253-57, 258(d).

35. *See id.* ¶ 128.

36. *See id.* ¶ 130-31.

37. *See id.* ¶ 132.

38. A third issue concerned the necessity analysis conducted by the Panel and Article 11 of the WTO *Understanding on Rules and Procedures Governing the Settlement of Disputes* (*Dispute Settlement Understanding*, or *DSU*). *See Brazil Tires* Appellate Body Report, *supra* note 25, ¶¶ 117(a)(ii), 184-209, 258(a)(ii). This issue was not central to the case and is not discussed below. Briefly, the Appellate Body found that the Panel did not fail to conduct an objective assessment of the facts of the case, as required by *DSU* Article 11, both as to the contribution of the Import ban in meeting its objective and in finding that the tire disposal methods suggested by the EC were not reasonably available alternatives to the Import Ban.

39. The discussion of the GATT Article XX(b) necessity issue below draws on *Brazil Tires* Appellate Body Report, *supra* note 25, ¶¶ 117(a)(i), 133-83, 258(a)(i).

40. The discussion of the GATT Article XX *chapeau* issue below draws on *Brazil Tires* Appellate Body Report, *supra* note 25, ¶¶ 117(b), 213-52, 258(b)-(c).

4. Step One of the Two Step Test: Necessity under GATT Article XX(b)

a. The Three Elements of "Necessity"

The Appellate Body affirmed the Panel decision on the issue of the Import Ban's necessity under GATT Article XX(b). The Import Ban indeed was "necessary to protect human, animal, or plant life or health." In reaching this conclusion, the Appellate Body stressed that there are three key elements, or inquiries, to defining "necessity." Taken together, they amount to a balancing test for "necessity." Indeed, each inquiry involves some degree of weighing and balancing.

First, what interests or values are at stake? That is, what is the policy goal the measure in controversy is supposed to serve—the end of the means? In this inquiry, the Appellate Body took pains to explain that GATT–WTO obligations are not as invasive as some critics contend. Perhaps it did so because many environmental organizations called on the EC to drop its claims against Brazil, criticizing the EC for trying to infringe on the sovereignty of Brazil as to public health and the environment.[41] The Appellate Body intoned that in respect of an Article XX(b) claim about health, each WTO Member has the sovereign right to determine the level of protection it considers necessary in a given context. There sometimes are ineluctable "tensions" between, on the one hand, international trade and, on the other hand, public health and environmental risks arising from waste generated by a traded product that is at the end of its useful life.[42] The right of each Member to place itself at a spot along the safety continuum is a "fundamental principle" under GATT–WTO law.[43]

Second, to what extent does the measure in dispute contribute to the policy goal the measure is supposed to achieve? No doubt, said the Appellate Body, "necessity" means "contribution[,]" but it does not mean "indispensable."[44] That much is plain, it said, from its precedent in *Korea – Various Measures on Beef*. The question to ask is whether a measure contributes to the achievement of its objective. In turn, a "contribution" exists if there is a "genuine relationship" between the "ends," or objective, of the measure and the "means" that measure embodies.[45] To assess whether the means adopted in a measure are

41. *See* Daniel Pruzin, *Environment: EU to Appeal WTO Ruling on Brazilian Ban on Retreaded Tires*, 24 Int'l Trade Rep. (BNA) 1123 (2007).

42. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 210.

43. *Id.*

44. *Id.*

45. *Id.*

genuinely related to achieving an end, the factors to examine are the end, the nature of the risk, and the level of protection from the risk sought. Most definitely, a measure does not have to be indispensable to the ends to be necessary. But, the measure does have to make a "material, not merely marginal or insignificant," contribution to achieving the objective—"especially if the measure at issue is as trade restrictive as an import ban."[46] (After all, no measure is as severe, in design or effect, as an outright prohibition on importation.) Put differently, defining "necessity" is an exercise in judicial balancing, where the scales of justice weigh the contribution of the measure to its objective against the trade restrictiveness of the measure.

Third, what alternatives to the measure at issue exist? Specifically, some consideration must be given to whether reasonably available alternatives exist to a trade restrictive measure.[47] Even if a measure is "necessary" in respect of the first two elements, *i.e.*, even if the analysis of the interests or values at stake and the contribution of the measure to achieving its objective yields a preliminary conclusion that the measure is "necessary," there could be an alternative way of achieving the policy goal at stake that has a less dramatically dampening effect on cross-border trade than the measure in controversy. If so, then that measure would not be necessary. Here, the Appellate Body cited its *Antigua Gambling* precedent for the proposition that a Member seeking to defend a measure as "necessary" need not prove there are no reasonably available alternatives to achieve its objectives. It also cited *Antigua Gambling* to define an "alternative" as a possible measure that (1) is less trade restrictive than the measure of the respondent in dispute, (2) preserves the level of protection desired and chosen by the respondent in respect of the policy objective being pursued, and (3) is reasonably available to the respondent, in the sense of not being merely theoretical in nature (*e.g.*, because the respondent is not capable of adopting it, or it would impose an undue burden, such as prohibitive costs or substantial technical difficulties). A possible measure that fails these criteria is not a genuine alternative.

b. Why Brazil's Import Ban was "Necessary"

In the case at bar, Brazil exercised its choice to safeguard its public and health against waste tires by adopting a policy objective—

46. *Id.*

47. *See id.* ¶¶ 210-11 (in the absence of "reasonably available alternatives").

reduction of the risks from the accumulation of waste tires to the maximum extent possible. Brazil had every right to do so and to declare as both vital and important in the highest degree the goal of protecting human life and health against dengue fever and malaria arising from the accumulation of waste tires. To achieve this objective, Brazil adopted an Import Ban. The Ban contributed materially, said the Appellate Body, to this objective: It helped reduce the number of waste tires in Brazil. In turn, the reduction of waste tires in Brazil helped cut risks to human, animal, and plant life and health arising from waste tires. The contribution, in brief, was necessary.

Why did the Import Ban contribute to cutting the number of waste tires in Brazil? Because of the Ban, imported retreaded tires were replaced either with (1) domestically retreaded tires made from tires used in Brazil (*i.e.*, retreaded tires made from local casings), or (2) new tires capable of future retreading (*i.e.*, new tires that are retreadable). In the first instance, when retreaded tires are manufactured in Brazil from tires used in Brazil, the retreading reduces accumulation of waste tires in Brazil.[48] Brazil has the production capacity for retreading, which does occur in Brazil, and Brazil has facilitated access for domestic retreaders to good-quality used tires. Retreading gives a second life to some used tires which otherwise would have become waste tires after their first and only life. The Ban also encourages domestic retreaders to retread more domestic used tires than they might otherwise have done, simply because consumers have no choice but to switch either to a retreaded tire produced domestically or to a new tire. As to the second instance, retreaded tires have a shorter lifespan than new tires. Thus, the Import Ban on retreaded tires reduced the total number of waste tires, insofar as new tires with a longer lifespan were used in place of imported retreaded tires. In fact, new tires sold in Brazil are of high quality, comply with international standards, and have the potential to be retreaded.

Why did the reduction in the number of waste tires, brought about by the Import Ban, contribute to a reduction of risks to human, animal, and plant life or health arising from waste tires? The essence of the problem is the accumulation of waste tires. Cutting this accumulation means cutting fertile breeding grounds for vectors of disease and tire fires. That is, in light of the significance of the interests

48. The Appellate Body observed that the prohibition on importing used tires and the CONAMA regulations on waste tire disposal operated in tandem with the Import Ban. These measures would help ensure demand for retreaded tires in Brazil is met by domestic retreaders, with those retreaders source domestic used tires as their raw material. *See Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 154.

that the Import Ban's policy objective protected, the Ban's contribution to achieving this objective outweighed the Ban's trade restrictiveness.

Further, there were no reasonably available alternatives to the Ban—contrary to the EC's argument. The EC suggested two categories of possible alternative measures, namely waste management and disposal, in lieu of the Import Ban. "Waste management" would include encouraging domestic retreading, improving the retreadability of tires, strengthening enforcement of the ban on imports of used tires, and enhancing implementation of existing collection and disposal schemes. "Waste disposal," urged the EC, would include co-incineration of waste tires, landfilling, recycling, and stock piling.

However, waste management and waste disposal are remedial measures. They deal with existing waste tires. The Import Ban is a preventive, non-generation measure seeking to cut down on the number of waste tires created. Waste management, in particular, could complement the Ban but could not substitute for it. Waste disposal is costly, risky, and could affect only a limited number of tires. For instance, landfilling of waste tires poses some of the same risks that Brazil sought to reduce through the Ban (*e.g.*, mosquito-borne diseases, tire fires, as well as instability of sites for future land reclamation and long-term leaching of toxic substances). It hardly could be considered a reasonably available alternative. Stockpiling is not a reasonably available alternative, because it does not dispose of waste tires. Incineration of waste tires presents health risks—the emission of toxic chemicals—even under strict emission standards. Only with the most up-to-date technology can the emissions be kept at minimum levels, and that technology is expensive. So, incineration is not a reasonably available alternative either. Finally, recycling waste tire material (including devulcanization and other forms of chemical or thermal transformation) is not a reasonably available alternative. It is costly (*e.g.*, because of the use of rubber asphalt), capable of disposing of only a small number of waste tires (*e.g.*, because of the use of rubber granulates), and in some instances of dubious safety from an engineering perspective.

Additionally, Brazil already had adopted some measures to reduce the accumulation of waste tires: encouraging domestic retreading, improving the retreadability of domestic used tires, and barring imports of used tires. These measures operated along with, not as substitutes for, the Ban. Similarly, Brazil had implemented some waste management measures, particularly collection and disposal schemes. Yet, they could not address all of the risks associated with waste tires. In sum, none of the suggestions put forth by the EC were reasonably available alternatives to Brazil's Import Ban.

c. Quantification is Not Necessary

In reaching its conclusion on necessity, the Appellate Body rejected the EC's argument that the Panel ought to have quantified the importance of the contribution of the Import Ban to the reduction of waste tires and risks. The EC faulted the Panel for reasoning in the abstract and for being content with the potential contribution the Ban could make. Surely more diligence—empirical evidence—was needed, the EC argued. Hard-headed empiricist philosophers like David Hume would have applauded, but the Appellate Body did not. The EC called for an unrealistically demanding standard. The Appellate Body had a precedent on point, the *EC Asbestos* case, in which it had declared that "a risk may be evaluated either in quantitative or *qualitative* terms."[49] The civil law country of Brazil was none too pleased to cite it.

For its part, the Appellate Body was none too happy to extend its precedent to the question of quantification of the contribution of a measure to the achievement of the objective of that measure. That is, *EC Asbestos* stands (*inter alia*) for the proposition that a risk need not be quantified. The Appellate Body said the same proposition applies to analyzing the relationship between the means and ends of a measure. In dealing with "complex public health or environmental problems," a "comprehensive policy" consisting of a "multiplicity of interacting measures" may be in order, and the contribution of any one single measure may not be "immediately observable," particularly in the short-term.[50]

Accordingly, there is no single way to decide whether a measure makes a material contribution to its objective. One possibility, which the Panel used in the *Brazil Tires* case, is to use past or present data. Another possibility is to rely on qualitative reasoning based on hypotheses that are supported by sufficient evidence. Still another possibility is to make quantitative projections into the future. Consequently, there was no need for the Panel either to quantify the contribution of the Import Ban to the reduction in the number of waste tires or to quantify the contribution of that reduction to the mitigation of risk.

---

49. *Id.* ¶ 138 (*quoting* Appellate Body Report, *European Community–Measures Affecting Asbestos and Asbestos-Containing Products* (Mar. 12, 2001) ¶ 167 [hereinafter *EC Asbestos* Appellate Body Report]); *see also id.* ¶ 146 (citing Appellate Body Report, *European Community–Measures Affecting Asbestos and Asbestos-Containing Products* ¶ 167).

50. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 151.

5. Step Two of the Two Step Test: The *Chapeau* to GATT Article XX

a. The Two Prongs of the *Chapeau* and the Underlying Philosophy of Good Faith

Of course, the problem for Brazil in the case at hand was that it could only justify the Import Ban provisionally under GATT Article XX(b). Brazil could not get the Ban through Step Two of the Two-Step Test. The Ban, in brief, flunked the *chapeau* of Article XX (effectively at the Panel stage, and definitely on appeal). Significantly, in holding that the Import Ban is not justified under the *chapeau*, the Appellate Body overturned not only certain particularized findings of the Panel but also the reasoning of the Panel. Regrettably, the Appellate Body's articulation of what the Article XX *chapeau* means, in terms of practical legal tests, is not as direct or clear as it ought to have been. Several paragraphs of discussion of the *chapeau* must be tolerated and then synthesized and distilled.

To begin, the Appellate Body identified the two key phrases of the *chapeau*. These two phrases create a two-pronged requirement for a provisionally justified measure to pass muster under the *chapeau*:

> 215. [T]he *chapeau's* requirements are two-fold. *First, a measure provisionally justified under one of the paragraphs of Article XX must not be applied in a manner that would constitute "arbitrary or unjustifiable discrimination" between countries where the same conditions prevail. Secondly, this measure must not be applied in a manner that would constitute "a disguised restriction on international trade."* Through these requirements, the *chapeau* serves to ensure that Members' rights to avail themselves of exceptions are exercised in good faith to protect interests considered legitimate under Article XX, not as a means to circumvent one Member's obligations towards other WTO Members.[51]

51. *Id.* ¶ 215. The Appellate Body cited its 1996 Report in *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R (Apr. 29, 1996) [hereinafter *Reformulated Gas*] and its 2005 Report in *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting*

What is the philosophy that underlies the two-pronged requirement? The Appellate Body answered:[52]

> 224. [in *U. S. – Turtle Shrimp*], the Appellate Body stated that "[t]he *chapeau* of Article XX is, in fact, but one expression of the *principle of good faith*." [53] The Appellate Body added that "[o]ne application of this general principle, the application widely known as the doctrine of *abus de droit*, prohibits the *abusive exercise of a state's rights* and enjoins that whenever the assertion of a right 'impinges on the field covered by [a] treaty obligation, it must be exercised *bona fide*, that is to say, reasonably.'"[54] Accordingly, the task of interpreting and applying the *chapeau* is "the delicate one of *locating and marking out a line of equilibrium* between the right of a Member to invoke an exception under Article XX and the rights of the other Members under varying substantive provisions (*e.g.*, Article XI) of the GATT 1994, so that neither of the competing rights will cancel out the other and thereby distort and nullify or impair the balance of rights and obligations constructed by the Members themselves in that Agreement."[55] The location of this line of equilibrium may move "as the kind and the shape of the measures at stake vary and as the facts making up specific cases differ."[56]

Services, WT/DS285/AB/R (Apr. 7, 2005) [hereinafter *Antigua Gambling*]. *Reformulated Gas* is discussed in RAJ BHALA, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE, *supra* note 32, at ch. 43. *Antigua Gambling* is treated in our *WTO Case Review 2005*, 23 ARIZ. J. INT'L & COMP. L. 107, 305-45 (2006).

52. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 224.

53. *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, at ¶ 154 (Oct. 12, 1998) [hereinafter *US – Turtle Shrimp*]. This case is discussed in BHALA, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE, *supra* note 32, at ch. 43.

54. *US – Turtle Shrimp, supra* note 53, ¶ 158 (quoting B. CHENG, GENERAL PRINCIPLES OF LAW AS APPLIED BY INTERNATIONAL COURTS AND TRIBUNALS 125 (Stevens & Sons, Ltd., 1953).

55. *US – Turtle Shrimp*, *supra* note 53, ¶ 159.

56. *Id.* ¶ 159.

The Appellate Body continued by reviewing how it has applied the two *chapeau* mandates, drawing the line between abusive and legitimate invocations of a GATT exception that it had drawn in previous cases.

b. Whether Discrimination is "Arbitrary" or "Unjustifiable" Depends on the Cause of that Discrimination

In its review of precedent, the Appellate Body made a subtle but critical conceptual shift. Moving from the grand level of the principle of good faith, and focusing on the first of the two prongs in the *chapeau*, the Appellate Body said that determining whether a provisionally justified measure discriminates in an "arbitrary" or "unjustifiable" manner requires an examination of the cause of that discrimination. The Appellate body explained:

> 225. Analyzing whether discrimination is arbitrary or unjustifiable usually involves an analysis that relates primarily to the *cause or the rationale of the discrimination*. Thus, we observe that, in *US – Gasoline*, the Appellate Body assessed the two explanations provided by the United States for the discrimination resulting from the application of the baseline establishment rules at issue. As it found them unsatisfactory, the Appellate Body concluded that the application of the baseline establishment rules resulted in arbitrary or unjustifiable discrimination. In [*US – Turtle Shrimp*], the Appellate Body relied on a number of factors in finding that the measure at issue resulted in arbitrary or unjustifiable discrimination. The assessment of these factors by the Appellate Body was part of an analysis that was directed at the cause, or the rationale, of the discrimination. *US – Shrimp (Article 21.5 – Malaysia)*[57] concerned measures taken by the United States to implement recommendations and rulings of the DSB in *US – Shrimp*. The Appellate Body's analysis of these measures under

57. *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW (Nov. 21, 2001) [hereinafter *US – Shrimp (Article 21.5 – Malaysia)*].

> the *chapeau* of Article XX focused on whether discrimination that might result from the application of those measures had a legitimate cause or rationale in the light of the objectives listed in the paragraphs of Article XX.[58]

---

58. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 225. As the Appellate Body explained in a footnote:

> The *US – Gasoline* case involved a programme aiming to ensure that pollution from gasoline combustion did not exceed 1990 levels. Baselines for the year 1990 were set as a means for determining compliance with the programme requirements. These baselines could be either individual or statutory, depending on the nature of the entity concerned. Whereas individual baselines were available to domestic refiners, they were not to foreign refiners.
>
> The first explanation provided by the United States for such discrimination was the impracticability of verification and enforcement of individual baselines for foreign refiners. ... Secondly, the United States explained that imposing the statutory baseline requirement on domestic refiners as well was not an option, because it was not feasible to require domestic refiners to incur the physical and financial costs and burdens entailed by immediate compliance with a statutory baseline.

Brazil Tires Appellate Body Report, *supra* note 25, ¶ 225 n.429.

Regarding the *US – Turtle Shrimp* case, the Appellate Body recalled in a footnote:

> These factors were: (i) the discrimination that resulted from a "rigid and unbending requirement" ... that countries exporting shrimp into the United States adopt a regulatory programme that is essentially the same as the United States' programme; (ii) the discrimination that resulted from the failure to take into account different conditions that may occur in the territories of other WTO Members, in particular, specific policies and measures other than those applied by the United States that might have been adopted by an exporting country for the protection and conservation of sea turtles ... ; (iii) the discrimination that resulted from the application of the measure was "difficult to reconcile with the declared policy objective of protecting and conserving sea turtles" ... , because, in some circumstances, shrimp caught abroad using methods identical to those employed in the United States would be excluded from the United States market; and (iv) the discrimination that resulted from the fact that, while the United States negotiated seriously with some WTO Members exporting shrimp into the United States for the purpose of concluding

> 226. The Appellate Body Reports in *US – Gasoline*, [*US – Turtle Shrimp*, and *US – Shrimp (Article 21.5 – Malaysia)* show that the analysis of whether the application of a measure results in arbitrary or unjustifiable discrimination *should focus on the cause of the discrimination, or the rationale put forward to explain its existence.*[59]

As a practical matter, to discern whether discrimination is "arbitrary" or "unjustifiable" under the Article XX *chapeau* requires an inquiry into the cause of the discrimination, meaning the justification for it put forth by the respondent.

c. What the Panel Said, and the EC Argued, on "Arbitrary" or "Unjustifiable" Discrimination

To see why the Import Ban did not pass muster under the *chapeau* according to the Panel, to see why the Appellate Body reversed certain specific findings of the Panel, and to understand much

---

> international agreements for the protection and conservation of sea turtles, it did not do so with other WTO Members . . . .

Brazil Tires Appellate Body Report, *supra* note 25, ¶ 225 n.431.

As for the *US Turtle Shrimp* Compliance Report, the Appellate Body observed:

> [T]he Appellate Body endorsed the panel's conclusion that conditioning market access on the adoption of a regulatory programme for the protection and conservation of sea turtles comparable in effectiveness – as opposed to the adoption of "essentially the same" regulatory programme – "allows for sufficient flexibility in the application of the measure so as to avoid 'arbitrary or unjustifiable discrimination . . . ." The Appellate Body also considered that the measures adopted by the United States permitted a degree of flexibility that would enable the United States to consider the particular conditions prevailing in Malaysia, notably because it provides that, in making certification determinations, the United States authorities "shall also take fully into account other measures the harvesting nation undertakes to protect sea turtles.

Brazil Tires Appellate Body Report, *supra* note 25, ¶ 225 n.432.

59. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 226 (Emphasis added).

of its rationale, it is useful to recall those specific findings and the Panel's chain of logic in support of them. It also is helpful to appreciate the EC's arguments against the Panel's findings and rationale. Briefly, the Panel said:

> • *The MERCOSUR Exemption does not result in "arbitrary" discrimination*
>
> The MERCOSUR Exemption did not result in "arbitrary" discrimination between countries in which the same conditions prevail. First, the Panel said the health impact of remoulded tires imported from MERCOSUR countries is comparable to that of remolded tires imported from the EC (or expectedly would be so). The MERCOSUR Exemption came only after Brazil lost a MERCOSUR arbitration case, suggesting Brazil was not motivated by capricious or unpredictable factors. The discrimination in favor of MERCOSUR countries was not *a priori* unreasonable. It occurred in the context of a customs union that was recognized by GATT Article XXIV as inherently providing preferential treatment to member countries. In other words, because the MERCOSUR arbitral ruling was a reasonable basis to enact the Exemption, by implication the resulting discrimination was not "arbitrary." That was true for the Panel, even though Brazil did not defend the MERCOSUR case on human health and safety grounds, and the Panel thought it inappropriate to assess the arguments Brazil made in that case.[60]
>
> • *The MERCOSUR Exemption does not result in "unjustifiable" discrimination*
>
> The MERCOSUR Exemption did not result in "unjustifiable" discrimination between countries where the same conditions prevail. The MERCOSUR Exemption would result in an "unjustifiably"

60. Both the Panel and Appellate Body observed that Brazil could have, but did not, justify the Import Ban under Article 50(d) of the *Treaty of Montevideo*, which says that no provision of that Treaty precludes protection of human, animal, and plant life and health. See *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 234.

discriminatory application of the Import Ban (as well as a disguised restriction on international trade) only to the degree the Ban actually resulted in import volumes of retreaded tires that significantly undermined the achievement of the Ban's objective. That had not occurred. Specifically, casings from non-MERCOSUR countries, as well as casings originally used in MERCOSUR, may be retreaded in any MERCOSUR country and then exported to Brazil as goods originating in MERCOSUR. Suppose the volume of such imports were so large that achieving the objective of the MERCOSUR Exemption were undermined significantly. In that case, application of the Exemption, in conjunction with the Import Ban, would be "unjustifiable" discrimination. However, import volumes of retreated tires under the Exemption were not significant, especially in a relative sense. Between 2002 and 2004, imports of retreaded tires under the Exemption increased by ten times, from 200 to 2,000 tons per year. But, before imposition of the Import Ban, Brazil imported 14,000 tons of retreaded tires per year from the EC.[61] Hence, the Exemption has not been applied in a manner that constituted "unjustifiable" discrimination.

• *The MERCOSUR Exemption is not a "disguised restriction"*

To date (i.e., up to the time of the Panel's examination), the MERCOSUR Exemption had not been applied in a manner that would constitute "a disguised restriction on international trade."

• *Used tire imports under court injunction render the Import Ban "unjustifiably" discriminatory*

Imports of used tires under Brazilian court injunctions have resulted in the Import Ban being applied in a manner that was "unjustifiably" discriminatory, and a "disguised restriction on

61. *See Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 220 n.417.

international trade," only to the extent these imports have been in such volumes as to undermine significantly the achievement of the Ban's objective. That is, imports of used tires under a court order enable Brazilian firms to produce retreaded tires domestically from imported casings, but retreaded tires produced abroad using the same casings cannot be imported into Brazil. The injunctions have led to "unjustifiable" discrimination. First, granting any injunction to permit used tire imports ran directly counter to the premise that used tire imports are forbidden. An injunction allows a used tire to enter Brazil before retreading, but not after. Second, quantitatively, the volume of imports of used tires under court order had been significant and thereby undermined Brazil's declared policy objective of reducing to the maximum extent possible risks from the accumulation of waste tires.

• *Used Tire imports under court injunction do not render the Import Ban "arbitrarily" discriminatory*

The imports of used tires under court injunctions had not resulted in "arbitrary" discrimination. Importation of used tires into Brazil was generally prohibited and occurred only in recent years via court order in specific cases. The associated discrimination could not be called "arbitrary" because the Brazilian courts did not act in a capricious or random way.

• *Used tire imports under court injunction render the Import Ban a "disguised restriction" on trade*

For essentially the same reason that the Import Ban is "unjustifiable" in its discrimination, it is a disguised restriction, too. Used tire imports occur in significant volumes. The beneficiary of those injunctions is the domestic retreading industry in Brazil. Through court order, that industry gets large amounts of used tires from MERCOSUR countries to use as material for its own activity, while competitor

> retreaders in non-MERCOSUR countries are kept out of the Brazilian market.

The EC, of course, appealed many of these Panel conclusions, as well as the supporting rationales.

For the EC, first, a measure is not "arbitrary" if it appears reasonable, predictable, and foreseeable. Surely, the MERCOSUR Exemption undermines the stated objective of the Import Ban and thus is unreasonable, contradictory – and "arbitrary." Second, the MERCOSUR tribunal did not obligate Brazil to create the Exemption. Brazil could have complied with the arbitral ruling by lifting the Import Ban for all third countries. Third, the quantitative test applied by the Panel for "unjustified" discrimination – relative import volumes – had no basis in GATT Article XX or in Appellate Body case law. That test is defective, moreover, because import volumes can and do fluctuate from year to year. Fourth, and more generally, the EC worried that if the obligations of a WTO Member under international agreements other than GATT–WTO texts are allowed to render discrimination that is held to be consistent with GATT Article XX, then the effectiveness of the Article XX *chapeau* will be seriously undermined. Put simply, the EC, though a party to a vast and growing number of RTAs, was concerned they would undermine multilateral agreements.

d. Why the Import Ban is "Arbitrary" or "Unjustifiable" in its Discrimination

In reversing the Panel decision, the Appellate Body held that the MERCOSUR Exemption resulted in an "arbitrary" or "unjustifiably" discriminatory application of the Import Ban under the Article XX *chapeau*. The Appellate Body explained why the Exemption was "arbitrary," "unjustifiable," or both, in discriminating against non-MERCOSUR retreaded tires:

> 227. We have to assess whether this explanation provided by Brazil is acceptable as a justification for discrimination between MERCOSUR countries and non-MERCOSUR countries in relation to retreaded tyres. In doing so, we are mindful of the function of the *chapeau* of Article XX, which is to prevent abuse of the exceptions specified in the paragraphs of that provision. . . . [T]here is such an abuse, and, therefore, there is arbitrary or unjustifiable

discrimination when a measure provisionally justified under a paragraph of Article XX is applied in a discriminatory manner "between countries where the same conditions prevail," and *when the reasons given for this discrimination bear no rational connection to the objective falling within the purview of a paragraph of Article XX, or would go against that objective*. The assessment of whether discrimination is arbitrary or unjustifiable should be made in the light of the objective of the measure. . . . [F]or example, that one of the bases on which the Appellate Body relied in US – *Shrimp* for concluding that the operation of the measure at issue resulted in unjustifiable discrimination was that one particular aspect of the application of the measure (the measure implied that, in certain circumstances, shrimp caught abroad using methods identical to those employed in the United States would be excluded from the United States market) was "difficult to reconcile with the declared objective of protecting and conserving sea turtles." Accordingly, we have difficulty understanding how discrimination might be viewed as complying with the *chapeau* of Article XX *when the alleged rationale for discriminating does not relate to the pursuit of or would go against the objective that was provisionally found to justify a measure under a paragraph of Article XX.*

228. In this case, the discrimination between MERCOSUR countries and other WTO Members in the application of the Import Ban was introduced as a consequence of a ruling by a MERCOSUR tribunal. The tribunal found against Brazil because the restriction on imports of remoulded tyres was inconsistent with the prohibition of new trade restrictions under MERCOSUR law. *In our view, the ruling issued by the MERCOSUR arbitral tribunal is not an acceptable rationale for the discrimination, because it bears no relationship to the legitimate objective pursued by the Import Ban that falls within the purview of Article XX(b), and even goes against this objective, to however small a degree.* Accordingly, we are of the view that *the*

> *MERCOSUR exemption has resulted in the Import Ban being applied in a manner that constitutes arbitrary or unjustifiable discrimination.*
>
> 229. The Panel considered that the MERCOSUR exemption resulted in discrimination between MERCOSUR countries and other WTO Members, but that this discrimination would be "unjustifiable" only if imports of retreaded tyres entering into Brazil "were to take place in such amounts that the achievement of the objective of the measure at issue would be significantly undermined." The Panel's interpretation implies that the determination of whether discrimination is unjustifiable depends on the quantitative impact of this discrimination on the achievement of the objective of the measure at issue . . . . [A]nalyzing whether discrimination is "unjustifiable" will usually involve an analysis that relates *primarily to the cause or the rationale of the discrimination.* By contrast, the Panel's interpretation of the term "unjustifiable" does not depend on the cause or rationale of the discrimination but, rather, is focused exclusively on the assessment of the *effects* of the discrimination. The Panel's approach has no support in the text of Article XX and appears to us inconsistent with the manner the Appellate Body has interpreted and applied the concept of "arbitrary or unjustifiable discrimination" in previous cases.[62]

Could the effects of discrimination be a relevant factor in determining whether the cause of discrimination is "justifiable"? Perhaps, agreed the Appellate Body. The *chapeau* of GATT Article XX deals with the manner in which a controversial measure is applied. But it is erroneous to do what the Panel did, *i.e.*, focus exclusively on the effects of discrimination to gauge whether that discrimination is "unjustifiable." The Panel got the test wrong, perhaps because it misunderstood the Appellate Body precedents or simply failed to apply them correctly.

Moreover, even discrimination that results from a rational decision, such as compliance with a MERCOSUR arbitral tribunal

---

62. *See id.* ¶¶ 227-29 (emphasis on "effects" original; all other emphases added).

ruling, can be "arbitrary." That happens when the discrimination is explained by a rationale that bears no relationship to the objective of the measure that is provisionally justified. Or, it occurs when the provisionally justified measure is orthogonal to that objective.

Simply put, for the Appellate Body, the MERCOSUR Exemption resulted in the Import Ban being "arbitrary or unjustifiable discrimination" under the *chapeau*.[63] The Panel was wrong to conclude that discrimination under the *chapeau* would be "unjustifiable" based solely on an analysis of relative import volumes of retreaded tire imports. The Panel was also wrong to find that the discrimination was not "arbitrary" just because the Exemption was supposed to implement a MERCOSUR tribunal decision.

e. The Second Prong of the *Chapeau*: A Disguised Restriction on Trade

Was the MERCOSUR Exemption a disguised restriction on international trade? The Panel thought not and ruled against the EC, which had argued that the Exemption diverts trade away from the EC and towards retreaders from other MERCOSUR countries. The Panel relied for its finding on the fact Brazil banned imports of both retreaded and used tires, in an effort to cut to the greatest extent possible the unnecessary accumulation of tires with short life spans. The Panel also drew on its reasoning from its discussion of "arbitrary" or "unjustifiable" discrimination, saying that the Import Ban would be applied in a manner that is a "disguised restriction on international trade" if imports from MERCOSUR countries occurred in significant amounts. Because the volume of imports of remoulded tires that actually occurred under the Exemption was insignificant, the Panel thought the Exemption was not a disguised trade restriction.

The Appellate Body agreed with the EC's contention that the Panel used essentially the same reasoning to assess the MERCOSUR Exemption and Import Ban under both prongs of the GATT Article XX *chapeau*. In both contexts, the Panel dwelled on the effects of the Exemption and Ban in terms of import volume. Only if the import volume under the Exemption were significant enough to undermine the objective of the Ban could the Ban be declared a disguised restriction. Not so, said the Appellate Body; the Panel's conclusion and logic was as faulty in the second prong analysis as it had been in the first prong analysis.

---

63. *See id.* ¶ 233.

Notably, however, the Appellate Body did not articulate a test for "disguised restriction on trade." Is the cause of the discrimination to be checked, as when ascertaining whether discrimination is "arbitrary" or "unjustifiable"? Or, are there some other criteria to be used? The Appellate Body left these questions unanswered.

f. Used Tire Imports Pursuant to Court Injunctions

What did the Appellate Body make of the Panel ruling that imports of used tires through Brazilian court injunctions constitute "arbitrary" or "unjustifiable" discrimination? The Appellate Body agreed with the conclusion of the Panel, but in a stronger form, and for different reasons.

The Appellate Body declared that importing used tires under court injunction actually goes against the objective pursued by the Import Ban. In so doing, the Ban was treated as "arbitrary," "unjustifiable" or both. But, the Appellate Body did not agree with the reasoning of the Panel, specifically its quantitative approach. The volume of imports that occur under court order does not matter in deciding whether the Ban is applied in an "unjustifiably" discriminatory manner. The court orders themselves could well be capricious or random and lead to "arbitrary" discrimination. Similarly, the Appellate Body reversed the Panel's finding that importing used tires through court injunctions results in an Import Ban being applied in a manner that is a "disguised restriction" on trade only to the extent that these imports are in such large volumes as to undermine the Ban's objective. The Appellate Body, again, did not like the quantitative approach of the Panel and felt that a "disguised restriction" could exist notwithstanding the significance of import volumes under court order.

In sum, the EC's victory over Brazil at the Panel stage was made more complete by the Appellate Body. More than just used tire imports under court injunction offended the *chapeau* to GATT Article XX. The Exemption itself, coupled with the Ban, could not pass that critical second step. Arguably, the EC victory also was deeper on appeal than at the previous level. That is because the Appellate Body laid out a clear test for "necessity" under Article XX(b) and accepted much of what the EC urged in respect of quantitative tests for determining whether discrimination is "arbitrary," unjustifiable," or a "disguised restriction" on trade under the *chapeau*.

6. Commentary

a. One Measure or Two?

The only modest analytical complexity in the Panel's finding and rationale was its treatment of the MERCOSUR Exemption under GATT Articles XI:1 and XX.[64] Should the Exemption and Import Ban be treated as two distinct measures? On the one hand, both existed in the same Brazilian law – Article 40 of Portaria SECEX 14/2004. Hence, the EC treated them as a combined measure. On the other hand, the Ban and the Exemption arose sequentially, the latter in 2002, only after the adverse MERCOSUR arbitral panel ruling. (In other words, the original ban, dating from 2000, did not contain an exception for MERCOSUR parties.)

The WTO Panel fudged the issue. For purposes of Article XI:1, the Panel treated the Import Ban and MERCOSUR Exemption as separate measures. Under Article XX(b), the Panel said the analysis should focus on the Ban itself, not elements extraneous to this measure such as situations in which the Ban is inapplicable (namely, the MERCOSUR Exemption). Yet, the Panel also said the Exemption is foreseen in the legal instrument containing the Import Ban. As a result, the Panel wound up including the Exemption in its analysis under the *chapeau* of Article XX.

The Appellate Body noted the Panel ought to have used a more holistic approach by examining together both elements of the same measure – the Import Ban and MERCOSUR Exemption in Article 40 of Portaria SECEX 14/2004. That way, said the Appellate Body, the Panel could have examined the combined measure for compliance with Article XI:1 and justification under Article XX(b). The Appellate Body did not overturn the Panel's reasoning, however. First, the EC did not appeal the Panel's analytical approach. Second, the Panel's methodology followed the outline of the pleadings by the EC.

The Appellate Body seems to have handled the question adroitly. It refrained from activism, limiting its ruling to matters within the pleadings and necessary to resolve the case at bar. It abjured a premature decision on combining versus differentiating measures, perhaps sensing that questions of combination or separation of measures must be resolved on a case-by-case basis. At the same time,

64. *See id.* ¶¶ 124-27.

its observations intimated righteous impatience with sloppy analysis. Panels are now on notice that in the future they must think through carefully the number of measures at issue, and how to apply GATT–WTO rules to them.

b. Weighing, Balancing, and Being a Judge

Concerning necessity, the EC argued unsuccessfully that the Panel had failed to weigh and balance the relevant factors under GATT Article XX(b).[65] How could the Panel have done so, when it did not quantify the contribution of the Import Ban to the objectives of that Ban? The argument is interesting, if not ironic. It was emblematic of what the EC expected: the Panel should weigh and balance, akin to common law judges, and the Panel had not been – well, dare it be said – sufficiently judge-like. Indeed, the argument signified what has become a truism of WTO adjudication but what in some circles can be politically incorrect to declare. Many cases, particularly under Article XX, involve old-fashioned, Anglo-American legal reasoning. Diplomats in venues like the General Council or Ministerial Conference cannot handle this process efficiently and might not be disposed to do so temperamentally.

The EC admitted that the Appellate Body never has defined "weighing and balancing" but urged that the term means assessing individually each relevant factor and examining the relative importance of all factors together to see if the challenged measure is necessary to secure the objective pursued. Brazil countered with the correct observation that Article XX(b) does not require contribution. The Appellate Body agreed and stepped in to elaborate on the meaning of "weighing and balancing":

> The weighing and balancing is a holistic operation that involves putting all the variables of the equation together and evaluating them in relation to each other after having examined them individually, in order to reach an overall judgment.[66]

A true common law court could not have made the point more clear. The Appellate Body finished on a point of precedent. Not only did the Appellate Body find no error in the work of the Panel but it also said

65. *See id.* ¶¶ 176-83.
66. *Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 182.

that the analysis of the Panel was squarely in line with four precedents on "necessity": the Appellate Body reports in *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, *Korea – Measures Affecting Imports of Fresh, Chilled, and Frozen Beef*, and *Dominican Republic – Import and Sale of Cigarettes*, as well as *Antigua Gambling*.[67]

c. Aims and Effects, Causes and Effects

To what extent is GATT–WTO jurisprudence on discrimination consistent, and need it be so? Consider jurisprudence under GATT Articles III and XX (national treatment and general exceptions, respectively). Under many GATT Article III:1-2 and III:4 precedents, it is clear that in deciding whether a measure is discriminatory, the aim of that measure is irrelevant.[68] Effects matter. Any tilting of the competitive playing field, whether *de jure* or *de facto*, whether actual or potential, is enough to justify a holding that a measure treats imports less favorably than like domestic products. Put a bit simplistically, it is not practicable to look into all the justifications given by national legislators for a controversial measure. Further, some legal systems represented in the WTO do not admit the use of legislative history. Moreover, politicians can say nearly anything to justify a measure, including swearing they did not intend any discriminatory effects.

Now turn to the *Brazil Tires* case. The Appellate Body explained that in determining whether the discrimination associated with a provisionally justified measure is "arbitrary" or "unjustified" requires an examination of the cause of that discrimination. The effects – at least in terms of the volume of trade – do not matter much, if at all.

---

67. *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R (Mar. 12, 2001) [hereinafter *EC – Asbestos*], *Korea – Measures Affecting Imports of Fresh, Chilled, and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R (Dec. 11, 2000) [hereinafter *Korea – Beef*], and *Dominican Republic – Import and Sale of Cigarettes*, WT/DS302/AB/R (Apr. 25, 2005) [hereinafter *Cigarette*]; *see Brazil Tires* Appellate Body Report, *supra* note 25, ¶ 182 n.327. *EC – Asbestos* and *Korea – Beef* are treated in our *WTO Case Review 2001*, 19 ARIZ. J. INT'L & COMP. L. 457, 472-517 (2002). *Cigarettes* is treated in our *WTO Case Review 2005*, 23 ARIZ. J. INT'L & COMP. L. 107, 118-30 (2006).

68. This jurisprudence is discussed in RAJ BHALA, MODERN GATT LAW: A TREATISE ON THE GENERAL AGREEMENT ON TARIFFS AND TRADE chs. 4-6 (2005).

Rather, the question is: What rationale is put forth to justify the discrimination? If the cause, or reason, for the discrimination bears no rational connection to the objective of the provisionally justified measure, or if the cause and objective are at cross-purposes, then the measure is "arbitrary" or "unjustified" in the way it discriminates. Here, the aim of a measure does matter.

To be sure, the issues arising under GATT Articles III and XX are different. With national treatment, the question is whether a measure is discriminatory. For general exceptions, the question is whether a discriminatory measure is justifiable. Nevertheless, is it sensible to forbid an inquiry into the aims of a measure in the first instance and require such an inquiry in the second instance? Is there a problem that categories of evidence that are unacceptable in the first context are admissible in the second context?

In *Brazil Tires*, the Appellate Body looked to what Brazil said, through its written and oral advocacy, to ascertain whether the cause of the discrimination associated with the MERCOSUR Exemption was an effort to comply with a ruling issued by a MERCOSUR arbitral panel. Suppose Brazil had offered, instead, legislative history, or statements from senior government officials, to explain its Exemption. That kind of evidence would not be persuasive if Brazil adduced it to show the Exemption created no national treatment problem. Indeed, that evidence would have been irrelevant to the question of whether the Exemption discriminates.

These challenges assume the "aims" of a measure and the "cause or rationale" of discrimination involve essentially the same inquiry. Whether they do needs careful thought.

d. Participation and Contingent Transparency

The Panel received two *amicus curiae* briefs – one from the Humane Society International, and one from an international coalition of non-governmental organizations (NGOs) comprised of the *Associação de Combate aos Poluentes* (Brazil), *Associação de Proteção ao Meio Ambiente de Cianorte* (APROMAC) (Brazil), the Center for Human Rights and the Environment (CEDHA) (Argentina), the Center for International Environmental Law (CIEL) (United States and Switzerland), *Conectas Direitos Humanos* (Brazil), Global Justice (Brazil), and the Law for a Green Planet Institute (Brazil).[69] Brazil included the *amicus* briefs as part of its exhibits. The Appellate Body,

69. *See Brazil Tires* Panel Report, supra *note* 25, § I, ¶ 8.

too, received two *amicus* briefs. The Humane Society International filed one, and a coalition of nine NGOs filed the other. (The nine were the aforementioned groups, plus Friends of the Earth Europe (Belgium) and the German NGO Forum on Environment and Development (Germany).) However, the Appellate Body declared "[t]he Appellate Body Division hearing the appeal *did not find it necessary* to take these *amicus curiae* briefs into account in rendering its decision."[70]

In respect of transparency, the CIEL asked the Panel to broadcast (via webcast) its proceedings.[71] However, the Panel declined. Interestingly, in a dispute between the United States and the EC on zeroing, the WTO announced on its website[72] on January 8, 2008 the following:

> *At the request of the parties in the dispute* "United States — Continued Existence and Application of Zeroing Methodology" (DS350), the Panel has agreed to start its meeting with the parties on 29 January 2008 with a session *open to public viewing at the WTO Headquarters in Geneva.* This public session is expected to start at 10.00 am on Tuesday, 29 January 2008 and the public viewing will take place via a real time closed-circuit television broadcast. The public session of the Panel meeting with the parties may continue at 3.00 pm on Wednesday, 30 January 2008, if the Panel so decides.
>
> With respect to the third parties session, which will be held on 30 January 2008 at 10.00, am, the Panel will start this session by opening a portion of it to public viewing. At this portion of the third parties session, third parties wishing to make their oral statements in a public session shall do so. Public viewing will also take place via a real time closed-circuit television broadcast.
>
> The number of places in the viewing room reserved for the public will be allocated on a first-come first-served basis *upon registration with either of the parties to the dispute i.e. the United States and the*

70. *Brazil Tires* Appellate Body Report, supra *note* 25, ¶ 7 (emphasis added).

71. *See Brazil Tires* Panel Report, supra *note* 25, § I, ¶ 9.

72. World Trade Organization, www.wto.org.

> *European Communities*. To register via either party, please click on the links below to be directed to the websites of the United States or the European Communities. The general public to whom seats have been allocated will need to present valid identification (passport) on-site to access the meeting room. Members of the public allocated a seat are requested to arrive in good time as security checks may delay access to the viewing room.
>
> Please note that any form of recording or filming is prohibited. As a courtesy to other participants, cell phones should be switched off during the public viewings.
>
> *The WTO cannot offer any support, including financial, for accommodation, flight arrangements and visas.*[73]

While this transparency is welcome, it is only a modicum of openness.

As the announcement indicates, there are many conditions to be met before a WTO proceeding can be observed. First, the parties must catalyze openness. If they do not agree, the proceeding will remain closed. That is because transparency is not yet an institutional feature of WTO dispute settlement but rather an ad hoc and episodic phenomenon. Second, one must be in Geneva. Students, scholars, and practitioners not there, for any reason – not the least of which may be the hefty cost of flying to and staying in what is consistently ranked as one of the world's most expensive cities[74] – are locked out. (Webcasting, of course, would help alleviate this problem.) Third, one must register with either of the parties. Whether that gives the parties the right to exclude an observer is uncertain. But, it again suggests that transparency is at the grace of the litigants, not at the core of the litigation process. In sum, there is contingent transparency.

---

73. *WTO Hearings on Zeroing dispute opened to the public*, WTO: 2008 News Items, *available at* http://www.wto.org/english/news_e/news08_e/dispute350_e.htm (emphasis added).

74. Among the ten most expensive cities in the world according to Mercer Human Resource Consulting Cost of Living Survey - Worldwide Ranking 2007 (including housing), *available at* http://www.mercer.com/costofliving#top50.

II. TRADE REMEDIES

A. Antidumping and Zeroing

1. Citation

United States – Measures Relating to Zeroing and Sunset Reviews, WT/DS294/AB/R (issued on 9 January 2007, adopted by the DSB on 23 January 2007) (complaint by Japan, with Argentina, China, European Communities, Hong Kong, India, Korea, Mexico, New Zealand, Norway, and Thailand as Third Parties).[75]

2. Facts and Panel Holdings[76]

Japan challenged the infamous zeroing methodology used by the United States Department of Commerce (DOC) in computing dumping margin.[77] The challenge was broad, concerning both Simple

---

75. Hereinafter, *Japan Zeroing* Appellate Body Report.

The Panel Report in the case is *United States – Measures Relating to Zeroing and Sunset Reviews*, WT/DS322/R (issued on 20 September 2006, adopted by the DSB as modified by the Appellate Body on 23 January 2007) (complaint by Japan, with Argentina, China, European Communities, Hong Kong, India, Korea, Mexico, New Zealand, Norway, and Thailand as Third Parties as Third Parties). Hereinafter, *Japan Zeroing* Panel Report.

76. This discussion is drawn from *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 1-6; *Japan Zeroing* Panel Report, *supra* note 75, ¶¶ 1.1-2.3; and World Trade Organization, *Update of WTO Dispute Settlement Cases*, WT/DS/OV/31 (Aug. 22, 2007) (Section V.A.3, discussion of *Japan Zeroing* case).

77. Japan also challenged the use of zeroing when ascertaining final duty liability for AD duties for entries of subject merchandise upon liquidation. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 1 n.2.

At the Panel stage, Japan made claims against the DOC's so-called "irrefutable presumption" in Sunset Reviews, and wavier provisions of United States AD law that obligate the DOC, in certain circumstances in a Sunset Review, to find a likelihood of continued or recurred dumping without engaging in a substantive examination review. These issues were not raised on appeal, and are not discussed herein.

Similarly, at the Panel Stage, Japan argued the DOC's Simple Zeroing methodology (both transaction-to-transaction and weighted average-to-transaction) was a "norm" that could be challenged as such in a WTO dispute settlement proceeding. The Panel agreed, and so did the Appellate Body. This issue, arising under Article 11 of the WTO *Understanding on Rules and Procedures Governing the Settlement of Disputes* (*Dispute Settlement*

and Model Zeroing in virtually all of their contexts. The key legal bases for the challenge were Articles 2:4 and 2:4:2 of the WTO *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (*Antidumping Agreement*),[78] Article VI:1-2 of the General

---

Understanding, or *DSU*), is not treated herein. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 62(a), 63-88, 181(a).

78. Article 2:4 of the *Antidumping Agreement* states:

> 2.4. A *fair comparison* shall be made between the export price and the normal value. This comparison shall be made at the same level of trade, normally at the ex-factory level, and in respect of sales made at as nearly as possible the same time. Due allowance shall be made in each case, on its merits, for differences which affect price comparability, including differences in conditions and terms of sale, taxation, levels of trade, quantities, physical characteristics, and any other differences which are also demonstrated to affect price comparability.78 In the cases referred to in paragraph 3, allowances for costs, including duties and taxes, incurred between importation and resale, and for profits accruing, should also be made. If in these cases price comparability has been affected, the authorities shall establish the normal value at a level of trade equivalent to the level of trade of the constructed export price, or shall make due allowance as warranted under this paragraph. The authorities shall indicate to the parties in question what information is necessary to ensure a fair comparison and shall not impose an unreasonable burden of proof on those parties. [Emphasis added.]

Article 2:4:2 of the *Antidumping Agreement* provides:

> 2.4.2. Subject to the provisions governing *fair comparison* in paragraph 4, the existence of margins of dumping during the investigation phase *shall normally* be established on the basis of a comparison of a *weighted average normal value with a weighted average of prices of all comparable export transactions or by a comparison of normal value and export prices on a transaction-to-transaction basis. A normal value established on a weighted average basis may be compared to prices of individual export transactions if* the authorities find a *pattern of export prices which differ significantly among different purchasers, regions or time periods*, and if an explanation is provided as to why *such differences cannot be taken into account* appropriately by the use of a weighted average-to-weighted average or transaction-to-transaction comparison.

[Emphasis added.]

Manifestly, Article 2:4:2 establishes three bases for comparison of Normal Value to Export Price. The first sentence sets out the weighted average-to-

Agreement on Tariffs and Trade (GATT), and Article XVI of the *Agreement Establishing the World Trade Organization* (*WTO Agreement*). The common sense basis for the challenge was fairness. Zeroing artificially inflates a dumping margin because it does not permit non-dumped sales to offset dumped sales.

Essentially, "zeroing" means disregarding the amount by which Export Price (or Constructed Export Price) exceeds Normal Value.[79] The DOC practices zeroing in original investigations of alleged dumping. It does so, too, in reviews of extant antidumping (AD) orders, namely, Changed Circumstances Reviews, New Shipper Reviews,[80] Periodic Reviews,[81] and Sunset Reviews. Zeroing is effected through one of two methodologies:

---

weighted average methodology (used in Model Zeroing), and the individual transaction-to-individual transaction methodology (*i.e.*, one of the two Simple Zeroing methods). These methodologies are symmetrical comparisons between Normal Value and Export Price. The Article clearly mandates – through the words "shall normally" – their use to establish a dumping margin. Only in exceptional circumstances is the third methodology (the second of the two Simple Zeroing methods), which the second sentence of Article 2:4:2 describes, to be used – an asymmetrical comparison between weighted average Normal Value and prices of individual export transactions (*i.e.*, individual Export Prices). The exceptional circumstances are: (1) an investigating authority finds the pattern of Export Prices differs significantly among purchasers, regions, or time periods (suggesting the possibility of targeted dumping, *i.e.*, aiming dumped merchandise at certain domestic producers of a like product, at specific areas of the importing country, or at particular times), and (2) these disparities cannot be accounted for by using either of the first two methodologies. *See also Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 122.

79. Hereinafter, reference to Export Price includes Constructed Export Price, as appropriate and relevant in a particular AD investigation. Zeroing methodologies, and examples thereof, are set out in BHALA, INTERNATIONAL TRADE LAW: INTERDISCIPLINARY THEORY AND PRACTICE, *supra* note 32, at ch. 32.

80. As its rubric connotes, a "New Shipper Review" is an inquiry about an exporter or foreign producer that did not export or produce subject merchandise during the period of investigation (POI) in the original investigation. The question is whether this new shipper – one that started exporting or producing subject merchandise after the original POI – is, in fact, dumping. Under Section 751(2)(B)(i)(II) of the *Tariff Act of 1930*, 19 U.S.C. § 1675(a)(2)(B)(i), in a New Shipper Review, the DOC must establishes a weighted average dumping margin for a particular new shipper.

81. Periodic Reviews are more commonly known in the United States as "Administrative Reviews." *See* §751(a) of the Tariff Act of 1930, *amended by* 19 U.S.C. § 1675(a)(2).

• Simple Zeroing entails a comparison for an entire product of either transaction-to-transaction (T-T) price data for Normal Value (from individual sales of a foreign like product) and Export Price (from individual sales of subject merchandise), or weighted average-to-transaction (W-T) price data for Normal Value (*i.e.*, a weighted average of sales prices for a foreign like product) and Export Price (from individual sales of subject merchandise). The comparisons, respectively, are sometimes labeled "individual-to-individual" and "average-to-individual." The individual-to-individual label indicates the methodology matches individual Normal Values from the home market of the exporter or foreign producer against the most appropriate individual Export Prices in the domestic (importing country) market. The average-to-individual label indicates the methodology matches weighted average Normal Value against individual Export Prices. Critically, if the dumping margin is negative for any T-T or W-T comparison, then the investigating authority sets that margin to zero. In the United States, the recalibration to zero occurs by operation of a specific line of computer programming code – the so-called "standard zeroing line" – in the AD Margin Calculation Computer Program, which is the software the DOC uses to calculate dumping margins.

• Model Zeroing entails a comparison of weighted average-to-weighted average (W-W) price data for Normal Value and Export Price across product sub-categories. (The comparison sometimes is referred simply as "average-to-average.") However, the single product category of subject merchandise is disaggregated into sub-product categories, also called "averaging groups," or "models." The division is based on physical characteristics of the product allegedly dumped. For each sub-product category, a weighted average Normal Value of the foreign-like sub-product is compared to the weighted average Export Price of the domestic-like sub-product. The overall dumping margin is the sum total of the

> dumping margins of the averaging groups. (Thus, Model Zeroing is also referred to as "multiple averaging," because the weighted average dumping margin for subject merchandise is computed from the multiple margins of the groups.) If the dumping margin is negative for any group, *i.e.*, if weighted average Export Price exceeds weighted average Normal value for any sub-product category, then that margin is set to zero. As with Simple Zeroing, the recalibration of a negative dumping margin to zero is effected via a standard zeroing line in the DOC's AD Margin Calculation Computer Program.

Japan brought suit against the United States in November 2004, contesting zeroing as such, and as applied by the DOC in one original investigation, eleven Periodic Reviews, and two Sunset Reviews.[82] The subject merchandise in the original investigation was cut-to-length carbon quality steel products made in Japan and exported to the United States. Given past Appellate Body precedents against zeroing, the result was predictable: Japan would win the case.[83] What was perhaps unforeseeable was the sweeping nature of its victory. On the key zeroing claims on which the United States prevailed at the Panel stage, the Appellate Body reversed.

The *Japan Zeroing* Panel agreed that Model Zeroing in original investigations is illegal under Article 2:4:2 of the *Antidumping Agreement*, ruling in favor of Japan's as such and as applied claims.[84] (The United States did not appeal this ruling,[85] in all likelihood because the DOC ceased the practice). But, in all other respects, the United States prevailed. Ruling against Japan's contention, the Panel held Simple Zeroing in original investigations did not violate the

---

82. The "as such" – "as applied" distinction is defined in RAJ BHALA, DICTIONARY OF INTERNATIONAL TRADE LAW (2008) (entries for those terms).

83. These precedents are set out in BHALA, DICTIONARY OF INTERNATIONAL TRADE LAW, *supra* note 82 (entry for "Zeroing," Table on Summary of WTO Precedents on Zeroing), and discussed in detail in previous *WTO Case Reviews*.

84. Interestingly, the Panel twice informed the Dispute Settlement Body (DSB) of delay – first on November 15, 2005 (that it could not compete its work within six months of its composition), and on May 10, 2006 (that it hoped to finish its work by August or September, which it did, circulating its Report on September 20, 2006). Both times the Panel cited the complexity of the issues as the reason for its delay.

85. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 90.

Antidumping Agreement (specifically, Articles 1, 2:1, 2:4, 2:4:2, 9:1-3, 9:5, and 18:4), *WTO Agreement* (Article XVI:4), or GATT (Article VI:1-2). The Panel also ruled for the United States, holding that Simple Zeroing, both as such and as applied, in Periodic Reviews and New Shipper Reviews, comported with GATT–WTO rules. In addition, the Panel found Japan failed to mount a *prima facie* case that zeroing in the context of Changed Circumstances and Sunset Reviews was illegal under Articles 2 and 11 of the *Antidumping Agreement.*

The Panel offered five justifications for its generally pro-zeroing Report:

> • First, aggregation –
>
> The *Antidumping Agreement* (specifically, Articles 2:1 and 2:4) can be interpreted as imposing no general obligation to determine a dumping margin for a product as a whole. The fact the *Agreement* refers to "dumping" and "margin of dumping" in relation to the term "product" or "products" does not prevent calculation of a dumping margin on the basis of an individual transaction. The *Agreement* does not mandate examination of the dumping margin at an aggregate level.[86]
>
> • Second, relevance –
>
> The *Antidumping Agreement* (specifically, Articles 2:1 and 2:4) does not mandate that the same weight be given to Export Prices that are above Normal Value, as is given to Export Prices that are below Normal Value. No inference in this regard can be drawn from the terms "dumping," "margin of

86. Article 2:1 of the *Antidumping Agreement* states:

> For the purpose of this Agreement, a product is to be considered as being dumped, *i.e.*, introduced into the commerce of another country at less than its normal value, if the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.

To overrule Panel findings about Article 2:1, the Appellate body relied on the same rationale it used to overturn Panel holdings concerning Article 2:4 and 2:4:2. That also is true in respect of GATT Article VI:1-2, about which there is little discussion in the Appellate Body Report. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 130-31.

dumping," "product," or "products." Indeed, there is logic in favor of the argument the *Antidumping Agreement* permits zeroing. Article 2:4:2 of the *Agreement* expressly condones use of individual-to-individual transaction comparisons of Export Price and Normal Value. Because dumping occurs whenever Export Price is below Normal Value, it may be rational to treat transactions in which Export Price is below Normal Value as more relevant than transactions in which Export Price exceeds Normal Value.

• Third, mathematical equivalence –

If zeroing was generally prohibited, then it would be logically impossible to reconcile the prophylactic ban with the express permission in Article 2:4:2 (second sentence) of the *Antidumping Agreement* to use a weighted average-to-transaction comparison methodology. Prohibiting zeroing in average-to-average, average-to-transaction, and transaction-to-transaction comparisons would render the average-to-individual method superfluous. That is, because mathematically average-to-transaction comparisons, without zeroing, necessarily yields the same result as average-to-average comparisons. (The United States argued, and the Panel agreed, that without zeroing, in an average-to-individual comparison, the sum total of the amounts by which Export Prices are above Normal Value would offset the sum total of the amounts by which Export Prices are less than Normal Value.[87]) In turn, the *Agreement* would have been read in a manner that violates effective treaty interpretation, thus, rendering a provision (the permission to engage in average-to-individual comparisons) redundant.

• Fourth, the text –

Nothing in the text of Article 2:4:2 of the *Antidumping Agreement* suggests that zeroing, while permissible for comparisons of weighted average

87. *See Japan Zeroing* Panel Report, *supra* note 75, ¶ 7.127 (including n.763).

> Normal Value against individual Export Price transactions, is forbidden for individual transaction comparisons of Normal Value to Export Price.
>
> • Fifth, fairness –
>
> The "fair comparison" requirement in the *Antidumping Agreement* (specifically, Article 2:4) is a general prescription. It cannot be read to override more specific rules, such as ones allowing transaction-to-transaction comparisons. To conclude zeroing yields an unfair comparison would render inoperative the specific permission to engage in transaction-to-transaction comparisons.

None of these justifications, even viewed most favorably to the Panel, is adamantine. Japan adroitly probed and spotlighted their weaknesses. On appeal, Japan's partial victory from the Panel stage became a complete one. Thee Appellate Body rendered key holdings – all reversing Panel holdings – on four critical topics, as discussed in parts 3-6, below.

3. Simple Zeroing in Original Investigations

First, the Appellate Body reversed the decision of the Panel that Simple Zeroing, using transaction-to-transaction comparisons of prices for Normal Value and Export Price, in original investigations, is legal.[88] To the contrary, said the Appellate Body, this methodology runs afoul of Article 2:4 and 2:4:2 of the *Antidumping Agreement.* Accordingly, the DOC application of this methodology violates those same provisions.

Japan urged that "dumping" and "margins" of dumping" must be calculated in relation to a product under investigation, subject merchandise, as a whole. In its summary of basic AD principles, the Appellate Body clearly hinted that it agreed with Japan:

> 106. A product under investigation may be defined by an investigating authority. But, "dumping" and "margins of dumping" can be found to exist only in relation to that product as defined by

88 *See Japan Zeroing* Appellate Body Report, *supra* note 75 ¶¶ 62(b), 89-138, 181(b).

> that authority. They cannot be found to exist for only a type, model, or category of that product. Nor, under any comparison methodology, can "dumping" and "margins of dumping" be found to exist at the *level* of an individual transaction. Thus, when an investigating authority calculates a margin of dumping on the basis of multiple comparisons of normal value and export price, the results of such intermediate comparisons are not, in themselves, margins of dumping. Rather, they are merely [quoting the Appellate Body Compliance Report, *United States – Final Determination on Softwood Lumber from Canada – Recourse to Article 21:5 of the DSU by Canada*, WT/DS264/RW at ¶ 87 (adopted 1 September 2006) (hereinafter, *U.S. – Softwood Lumber V* Appellate Body Compliance Report] "inputs that are [to be] aggregated in order to establish the margin of dumping of the product under investigation for each exporter or producer."[89]

Moreover, argued Japan, the "fair comparison" requirement, in Article 2:4, is not subject to specific rules in the *Agreement*, but rather is an over-arching requirement that an investigating authority must respect in all its calculations in any AD proceeding. Yet, Simple Zeroing in original investigations effectively leads to only a sub-part of subject merchandise being addressed in a dumping margin calculation, and thereby artificially inflates the margin.

The United States countered unsuccessfully that the Panel had gotten matters right – the terms "dumping" and "margin of dumping" do not require aggregation of results from transaction-to-transaction comparisons, nor do they mandate offsetting one transaction (*e.g.*, a non-dumped sale) against another (*e.g.*, a dumped sale); zeroing does not artificially inflate a dumping margin, but rather produces the correct magnitude of dumping, because the argument of unfairness is predicated on the assumption zeroing is prohibited in transaction-to-transaction comparisons.

However, the American defense foundered on logic. The essence of that defense was that an investigating authority, when aggregating transaction-specific results, may disregard transactions in which Export Price is above Normal Value because those transactions

89. *Id.* ¶ 106 (emphasis in original).

do not involve dumping. Yet, as the Appellate Body explained, the American defense fundamentally confuses what a dumping margin is:

> 117. . . . [T]he *Anti-Dumping Agreement* requires the determination of an individual margin of dumping for each known exporter or foreign producer. If it is permissible to determine a separate margin of dumping for each transaction, the consequence would be that several margins of dumping could be found to exist for each known exporter or foreign producer. The larger the number of export transactions, the greater the number of such transaction-specific margins of dumping for each exporter or foreign producer. This would create uncertainty and divergences in determinations to be made in original investigations and subsequent stages of anti-dumping proceedings.[90]

To say, as the United States argued,[91] that a transaction does not involve dumping because the Export Price of subject merchandise exceeds the Normal Value of a foreign like product to which the merchandise is matched is incorrect. It simply makes little sense (to speak of separate dumping margins for specific transactions, other than possibly to illustrate what dumping is for pedagogical purposes. (Similarly, it is not sensible to speak of the terms "product" or "products" as applying to a single transaction). The theoretical appeal of the concept of a dumping margin is enhanced when that concept is tied to subject merchandise. The practical reliability of the concept is enhanced when it is measured by a large number of sales of a foreign-like product in the home market of the exporter or foreign producer matched against sales of a domestic-like product in the importing country. Simply put, transactions are not dumped; rather, goods are dumped, and the more observations of dumping, the greater the confidence in a conclusion that goods are in fact being dumped.

It is, moreover, illogical to think of a dumping margin in relation to a specific transaction given that only injurious dumping is actionable under GATT–WTO rules. Only if dumping of subject merchandise causes injury may a remedial AD duty be imposed. One of three key factors necessary for an injury determination is the volume of dumped imports (the other two are price and other relevant variables).

---

90. *Id.* ¶ 117.
91. *See id.* ¶ 118.

How could it be logical to exclude certain transactions from the dumping margin calculation, yet take those same transactions into account when evaluating injury? In effect, the same transactions would be treated as non-dumped when computing the margin, but as dumped when determining injury. The result hardly would be consistent – and, the Appellate Body would have done well to add- fair-treatment of subject merchandise.[92]

The American defense also foundered on precedent. The Appellate Body recalled its finding in the *U.S. – Softwood Lumber V* Appellate Body Compliance Report, the first instance in which it dealt with Simple Zeroing through T-T comparisons in original investigations. In that case, the Appellate Body explained that Article 2:4:2 (first sentence) refers to "a comparison" in the singular, which suggests the overall dumping margin calculation is an exercise requiring aggregation of multiple transactions. Each transaction-specific result (*i.e.*, each individual comparison of Normal Value to Export Price) merely is a step in the comparison process, an input into that process – not a final result in the calculation. The T-T methodology is a multi-step exercise, one involving many inputs that ultimately are aggregated to produce a single dumping margin for subject merchandise for each exporter or foreign producer. Critically, quoting from its Compliance Report, the Appellate Body wrote in *Japan Zeroing*: "[We held that] in aggregating the results of transaction-specific comparisons, "an investigating authority must consider the results of all of the comparisons and may not disregard the results of comparisons in which export prices are above normal value."[93]

Unsurprisingly, the Appellate Body intoned in the next paragraph of its *Japan Zeroing* Report:

> We see no reason to depart from the Appellate Body's reasoning in *U.S. – Softwood Lumber V (Article 21:5 – Canada)*, which is in consonance with the Appellate Body's approach in the earlier case of *U.S. – Softwood Lumber V* [*i.e.*, Appellate Body Report, *United States – Final Dumping Determination on Softwood Lumber from Canada*, WT/DS264/AB/R (adopted 31 August 2004)[94]] and is consistent with the fundamental disciplines that apply under the *Anti-Dumping Agreement* and Articles VI:1

92. *See id.* ¶ 119.
93. *Id.* ¶ 111.
94. This case is treated in our *WTO Case Review 2004*.

> and VI:2 of the GATT 1994.... In the latter case, the Appellate Body held that, "[i]f an investigating authority has chosen to undertake multiple comparisons, the investigating authority necessarily has to take into account the results of *all* those comparisons in order to establish margins of dumping for the product as a whole under Article 2:4:2."[95]

To be sure, the Appellate Body distinguished its *Softwood Lumber V* precedent. The earlier case also involved an original investigation, Model Zeroing using the W-W comparison. But, in the case at bar, Japan challenged use by the DOC of Simple Zeroing (using the T-T method) in an original investigation. Nevertheless, the distinction was without a material difference.

In Model Zeroing, the DOC zeroed any intermediate value for a product sub-category if Export Price exceeded Normal Value. That is, zeroing occurred not within model groups, but rather across models of the product at issue. When aggregating the values of all the models, the DOC set to zero the value for any model for which the value was negative (in effect, for which no dumping occurred). In *Softwood Lumber V*, the Appellate Body stressed that a comparison between Export Price and Normal Value within a product sub-category is not itself a dumping margin. Technically, it is erroneous to speak of a dumping margin other than in relation to a product as a whole. That said, if Model Zeroing is inconsistent with Article 2:4:2 of the *Antidumping Agreement*, then *a fortiori* Simple Zeroing is, too:

> 114. We fail to see why, if, for the purpose of establishing a margin of dumping, such a product is dealt with under the T-T comparison methodology in an original investigation, zeroing would be consistent with Article 2:4:2 of the *Anti-Dumping Agreement. If anything, zeroing under the T-T comparison methodology would inflate the margin of dumping to an even greater extent as compared to model zeroing under the W-W comparison methodology.* This is because zeroing under the T-T comparison methodology disregards the result of each comparison involving a transaction in which the export price exceeds the normal value, whereas under

95. *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 112 (emphasis in original).

> the W-W comparison methodology, zeroing occurs . . . only across the sub-groups in the process of aggregation.[96]

Here, then, was an argument to which the United States simply had no rebuttal.

Nor could the American side justify the asymmetry that would occur if Simple Zeroing were permitted using the T-T method, but Model Zeroing using W-W comparisons were forbidden. Article 2:4:2 (first sentence) of the *Antidumping Agreement* sets out the T-T and W-W procedures, condoning both with equal vigor, but establishing no preference as between them. (Rather, the preference is between T-T and W-W, on the one hand, over W-T, on the other hand.) Ruling against Japan would create a hierarchy between the T-T and W-W methods, with W-W getting the top spot because an investigating authority could use zeroing in that instance. In turn, in a single investigation with the same data, a different dumping margin could occur – a larger one if calculated by a W-W comparison, and a smaller one if computed by a T-T comparison.

What did the Appellate Body make of the Panel's argument concerning mathematical equivalence (the fourth of the Panel justifications bulleted above, concerning redundancy between the W-W and W-T methodologies)? Once again, the Appellate Body trotted out a precedent—the *U.S.-Softwood Lumber V* Compliance Report. The Appellate Body had considered the same issue in that Report, and rejected the argument for good reason. First, one provision of an Article in a WTO text is not rendered entirely inutile simply because its application would yield, in a specific set of circumstances, the same result as the application of another provision in the same Article. A conclusion of total redundancy is excessively broad, because redundancy occurs only in limited instances. Second, the mathematical equivalence argument is in support of allowing zeroing under the T-T methodology, yet it rests on a presumed equivalence of the W-W and W-T methodologies. In other words, the argument contains a *non-sequitur*. Third, the mathematical equivalence argument itself depends on assumptions that are not universally valid; those assumptions depend on context.

In *Japan Zeroing*, the Appellate Body added one more good reason for rejecting the Panel's view that, if zeroing is allowed in a W-T comparison, then it should be allowed in a T-T comparison. In a W-T case, an investigating authority is trying to uncover whether targeted

---

96. *Id.* ¶ 114 (emphasis added).

dumping occurs. Article 2:4:2 of the *Antidumping Agreement,* thus, speaks of a "pattern of export prices which differ significantly among different purchasers, regions, and time periods." Because of the word "pattern," the authority is not compelled to rely on all data about export transactions to compute a dumping margin. Rather, the word allows it to "unmask targeted dumping" by examining only "the prices of export transactions falling within the relevant pattern."[97]

In another important respect, the American defense ran up against Appellate Body precedent. On whether Simple Zeroing in original investigations produces an artificially inflated dumping margin, and therefore, is not a fair comparison between Normal Value and Export Price, the United States essentially asserted, "no, zeroing yields the correct magnitude."[98] If there was a time in WTO litigation to bring the force of legal philosophy and comparative jurisprudence to bear, the appellate phase of the *Japan Zeroing* case was it. Regrettably, the United States appeared to make no imaginative arguments of the sort.

Instead, the United States cited an Appellate Body Report [99] recognizing a need to balance rights and obligations of respondents and other interested parties in an AD proceeding, adding that a domestic industry is an interested party. In doing so, the United States met head-on a better precedent – the *Softwood Lumber V Appellate Body Compliance Report.* In quoting from the *Compliance Report*, the *Japan Zeroing* Appellate Body almost seemed to lecture the United States:

> 137. The Appellate Body has previously made it clear that the use of zeroing under the T-T comparison methodology distorts the prices of certain export transactions because the "prices of [certain] export transactions [made] are artificially reduced." In this way, "the use of zeroing under the [T-T] comparison methodology artificially inflates the magnitude of dumping, resulting in margins of dumping and making a positive determination of dumping more likely." The Appellate Body has further stated, "[t]his way of calculating cannot be described as impartial, even-handed, or unbiased." As the Appellate Body has previously found, under the first sentence of

97. *Id.* ¶ 126.

98. *Id.* ¶ 136 (citing the American appellate brief).

99. *United States – Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina*, WT/DS268/AB/R (Nov. 29, 2004). This case is treated in our *WTO Case Review 2004.*

> Article 2:4:2, "an investigating authority must consider the results of all the comparisons and may not disregard the results of comparisons in which export prices are above normal value." Therefore, we consider that zeroing in T-T comparisons in original investigations is inconsistent with the fair comparison requirement in Article 2:4.[100]

Here, then, was a squandered opportunity.

The United States might have plucked from the annals of legal philosophy a powerful theory about fairness or about the rule of law.[101] Perhaps in a dusty old law book there is a theory that justice demands greater weight to be given to a transgression (Normal Value exceeding Export Price) than to the happenstance of good behavior (Export Price exceeding Normal Value). The United States might have explored comparative jurisprudence for treatment of mitigating circumstances in other legal fields and systems. Perhaps there are compelling illustrations of administrative or judicial discretion as to whether mitigating circumstances (akin to non-dumped sales of subject merchandise) may offset an injurious offense (akin to dumped sales).

Certainly, there is no guarantee the Appellate Body would have accepted a scholarly American argument about fairness that drew on legal philosophy or comparative jurisprudence. Had it done so, the United States would have succeeded magnificently. Had it rejected such an argument, at least the United States would have failed grandly.

---

100. *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 137 (parenthetical insertions added by the Appellate Body).

101. Among many possibilities, here are eleven books that might be (or might have been) worth consulting: BRIAN BIX, JURISPRUDENCE:THEORY AND CONTEXT (2d ed. 1999); EDGAR BODENHEIMER, TREATISE ON JUSTICE (1967); EDGAR BODENHEIMER, JURISPRUDENCE:THE PHILOSOPHY AND METHOD OF THE LAW (rev'd ed. 1974); THE OXFORD HANDBOOK OF JURISPRUDENCE AND PHILOSOPHY OF LAW (Jules Coleman & Scott Shapiro, eds., 2002); M.D.A. FREEMAN, LLOYD'S INTRODUCTION TO JURISPRUDENCE (6th ed. 1994); J.M. KELLY, A SHORT HISTORY OF WESTERN LEGAL THEORY (1992); THE GREAT LEGAL PHILOSOPHERS:SELECTED READINGS IN JURISPRUDENCE (Clarence Morris ed., 1959); GEORGE W. PATON, A TEXTBOOK OF JURISPRUDENCE (George W. Paton & David P. Derham, eds., 4th ed. 1972); ROSCOE POUND, AN INTRODUCTION TO THE PHILOSOPHY OF LAW (rev. ed. 1954); JOHN RAWLS, A THEORY OF JUSTICE (rev. ed. 1999); WHAT IS JUSTICE? CLASSIC AND CONTEMPORARY READINGS (Robert C. Solomon & Mark C. Murphy eds., 1990).

4. Zeroing in Periodic Reviews

The second key holding of the Appellate Body – again reversing the Panel – concerned Periodic Reviews. The Appellate Body ruled zeroing in Periodic Reviews is unlawful under Articles 2:4 and 9:3 of the *Antidumping Agreement* and under Article VI:2 of GATT.[102] Accordingly, the eleven Periodic Reviews cited by Japan all were

---

102. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 62(c), (e), 139-157, 163-168, 181(c), (e).

Article 9:3 of the *Antidumping Agreement* states:

> 9.3. The amount of the anti-dumping duty shall not exceed the margin of dumping as established under Article 2.
>
> 9.3.1. When the amount of the anti-dumping duty is assessed on a retrospective basis, the determination of the final liability for payment of anti-dumping duties shall take place as soon as possible, normally within 12 months, and in no case more than 18 months, after the date on which a request for a final assessment of the amount of the anti-dumping duty has been made.102 Any refund shall be made promptly and normally in not more than 90 days following the determination of final liability made pursuant to this sub-paragraph. In any case, where a refund is not made within 90 days, the authorities shall provide an explanation if so requested.
>
> 9.3.2. When the amount of the anti-dumping duty is assessed on a prospective basis, provision shall be made for a prompt refund, upon request, of any duty paid in excess of the margin of dumping. A refund of any such duty paid in excess of the actual margin of dumping shall normally take place within 12 months, and in no case more than 18 months, after the date on which a request for a refund, duly supported by evidence, has been made by an importer of the product subject to the anti-dumping duty. The refund authorized should normally be made within 90 days of the above-noted decision.
>
> 9.3.3. In determining whether and to what extent a reimbursement should be made when the export price is constructed in accordance with paragraph 3 of Article 2, authorities should take account of any change in normal value, any change in costs incurred between importation and resale, and any movement in the resale price, which is duly reflected in subsequent selling prices, and should calculate the export price with no deduction for the amount of anti-dumping duties paid when conclusive evidence of the above is provided.

instances in which the United States acted inconsistently with its WTO obligations.[103]

On appeal, Japan successfully argued that a dumping margin must be established for an exporter or foreign producer in a manner consistent with the *Antidumping Agreement* so as to ensure the amount of duties collected does not exceed the margin. Here again, a "fair comparison" is needed. The United States, of course, urged the Appellate Body to see the wisdom of the Panel Report – nothing in Article 9:3 commands aggregate examination of export transactions to determine final liability for payment or refund of AD duties.

To support its finding, the Panel largely relied on reasoning it used to back its conclusion that zeroing is permissible in original investigations. It extended that reasoning, where relevant, from Articles 2:1, 2:4, and 2:4:2 to Articles 9:1-9:3 and 9:5 of the *Antidumping Agreement*. Most notably, the Panel said the terms "dumping" and "margin of dumping," as used in Article 9, apply to results of transaction-specific comparisons. The Appellate Body easily cut down the Panel reasoning. In a blissfully brief paragraph,[104] it recalled its finding in respect of Simple Zeroing in original investigations – the terms "dumping" and "margins of dumping" are meaningful only at the level of a "product," not at the level of a type, model, or sub-category of product, nor at the level of an intermediate transaction, and whenever dumping margin is calculated on the basis of multiple comparisons at an intermediate stage, only by aggregating all intermediate results can a dumping margin be established for a product as a whole.

The Appellate Body also rejected the reasoning offered by the Panel peculiar to Articles 9:3:1 and 9:3:2 of the *Antidumping Agreement*, which respectively concern calculation of a dumping margin for final liability for AD duties in a retrospective system (like

---

103. In the eleven Periodic Reviews, the DOC assessed AD duties using zeroing and the W-T methodology. For each individual importer, the DOC compared Export Price of each individual transaction made by that importer against a contemporaneous average Normal Value. The DOC then took the results of the multiple comparisons, aggregated them, and thereby obtained the AD duty liability of each individual importer. But, for any particular individual transaction, if Export Price exceeded the contemporaneous average Normal Value, then the DOC – at the aggregation stage – disregarded the result of this transaction. By disregarding systematically transactions in which Export Price was above Normal Value, the DOC collected AD duties in excess of the "proper" dumping margin relating to sales by an exporter or foreign producer. *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 166.

104. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 142.

the United States)[105] and calculation of a dumping margin to establish any refund in a prospective duty assessment system.[106] The Panel read

---

105. The Appellate Body allayed the Panel's concern that in a retrospective duty assessment system, an investigating authority might be precluded from collecting an AD duty in respect of export transactions at prices less than Normal Value to a specific importer, because prices of export transactions to other importers at a different time exceed Normal Value. That concern is unfounded, said the Appellate Body, because it fundamentally misconstrues what dumping is all about. Dumping concerns the behavior of an exporter or foreign producer. It is the exporter or foreign producer, not the importer, which engages in pricing practices that result in dumping. At the time of importation of subject merchandise, AD duties may be collected in the form of a cash deposit on all export sales, including any occurring at above Normal Value. Then, in a Periodic Review under Article 9:3:1 of the *Antidumping Agreement*, the relevant authority must:

> ensure that the total amount of anti-dumping duties collected from all the importers of that product does not exceed the total amount of dumping found in *all* sales made by the exporter or foreign producer, calculated according to the margin of dumping established for that exporter or foreign producer without zeroing.

Japan Zeroing Appellate Body Report, *supra* note 75, ¶ 147 (emphasis in original). Indeed, the above-quoted response from the Appellate Body seems so obvious that it is perhaps surprising the Panel would be concerned about the matter.

106. Still, another concern the Appellate Body allayed in the context of Periodic Reviews concerned prospective normal value systems. In a prospective normal value system, the relevant governmental authority announces a "Prospective Normal Value" before collecting any AD duties. The Prospective Normal Value applies to future entries of subject merchandise. The authority assesses AD duties on the basis of the difference between Prospective Normal Value and the prices of individual export transactions (*i.e.*, Export Price or Constructed Export Price) for the merchandise. In a prospective normal value system, an exporter or foreign producer may decide to raise its Export Prices to the level of Prospective Normal Value, and thereby avoid liability for payment of an AD duty on each export transaction for which it raised Export Price.

While a refund of any excess duties occurs later, following Article 9:3:2 of the *Antidumping Agreement*, in a prospective normal value system, liability for payment of AD duties is final at the time of importation of subject merchandise. In this system, does the AD duty collected at the time of importation represent a "margin of dumping?" Can the total amount of AD duties levied in such a system exceed the "margin of dumping" for an exporter or foreign producer? To both questions, the Appellate Body said, the answer is "no."

these provisions, along with GATT Article VI:2, to mean there is no general requirement to determine a dumping margin for a product as a whole without using zeroing. The Panel said the obligation to pay an AD duty, or entitlement to a refund of an AD duty, is on an importer- and import-specific basis. If certain export sales to a particular importer are made at prices above Normal Value, then those sales do not need to be taken into account when computing the dumping margin for the relevant exporter that made the sales to that importer.[107]

Not so, said the Appellate Body. Once again, a precedent resolved the matter – the Appellate Body Report in *U.S. Zeroing (EC)*.[108] Article 9:3 of the *Antidumping Agreement*, and Article VI:2 of GATT, simply require an investigating authority to ensure that the total amount of AD duties collected on entries of subject merchandise from a given exporter does not exceed the dumping margin from that exporter. The dumping margin established for an exporter or foreign producer is

---

The Panel reasoned that in a prospective normal value system, liability to pay AD duties is incurred only to the extent that prices of individual export transactions are less than Normal Value. Therefore, thought the Panel, under Article 9:4(ii), the concept of "dumping" and a "margin of dumping" can apply on a transaction-specific basis to a price of an individual export transaction that is below Normal Value. Moreover, in a prospective normal value system, liability for an AD duty is triggered whenever the price of an individual export transaction is below the Prospective Normal Value, regardless of other export transactions in which the price exceeds Prospective Normal Value. That was a kind of zeroing – disregarding transactions above the benchmark of Prospective Normal Value. Why then, asked the Panel, should zeroing be forbidden in a retrospective system, such as that used by the United States?

In overruling the Panel, the Appellate Body gave a simple answer: in both prospective and retrospective systems, duty liability may be assessed on a transaction-specific basis, but the margin of dumping must be established in accordance with Article 2 of the *Antidumping Agreement*; that margin is the ceiling for the amount of AD duties that can be collected in respect of sales made by an individual exporter or foreign producer; and duties paid in excess of that ceiling may be claimed by the importer as a refund. In sum, the Agreement is neutral as to whether a WTO Member should adopt a prospective or retrospective system for the collection of AD duties, favoring neither over the other. The critical disciplines are on the establishment of the dumping margin for an exporter or foreign producer, the use of that margin as a ceiling on collection of duties associated with sales made by that exporter or foreign producer and the entitlement of an importer to a refund of excess duties. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 148-54.

107. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 145.

108. *United States – Laws, Regulations and Methodology for Calculating Dumping Margins*, WT/DS294/AB/R (Apr. 18, 2006). This case is treated in our *WTO Case Review 2006*.

a ceiling for the total amount of AD duties that can be levied on entries from that exporter. Certainly, these Articles do not prescribe a single methodology as to how to assess duties. They impart discretion to an investigating authority, as to assessing AD duties on a transaction-specific or an importer-specific basis, and as to a methodology appropriate for the nature and purposes of the proceeding. But, the key constraint is any AD duty assessed must not exceed the dumping margin for an exporter or foreign producer. The problem with zeroing is that it causes this constraint to be breached. Zeroing inflates the dumping margin, leading to an assessment in excess of the true margin.[109]

5. Zeroing in New Shipper Reviews

The Appellate Body had little reason to say much about zeroing in New Shipper Reviews. Japan essentially reiterated its winning arguments in this context, as it had made for Periodic Reviews. The United States said the Panel had read Article 9:5 of the *Antidumping Agreement* correctly[110] – its text does not imply "individual margins of dumping" are necessarily a "single" dumping

109. To cinch this final step, the Appellate Body might have been a little clearer about this point, though a careful re-reading of the relevant paragraphs – 146 and 147 – brings out the idea.

110. Article 9:5 of the *Antidumping Agreement* states:

> If a product is subject to anti-dumping duties in an importing Member, the authorities shall promptly carry out a review for the purpose of determining individual margins of dumping for any exporters or producers in the exporting country in question who have not exported the product to the importing Member during the period of investigation, provided that these exporters or producers can show that they are not related to any of the exporters or producers in the exporting country who are subject to the anti-dumping duties on the product. Such a review shall be initiated and carried out on an accelerated basis, compared to normal duty assessment and review proceedings in the importing Member. No anti-dumping duties shall be levied on imports from such exporters or producers while the review is being carried out. The authorities may, however, withhold appraisement and/or request guarantees to ensure that, should such a review result in a determination of dumping in respect of such producers or exporters, anti-dumping duties can be levied retroactively to the date of the initiation of the review.

margin determined from a "product as a whole" for each exporter or foreign producer. The Panel did not provide a separate interpretative discussion on New Shipper Reviews, i.e., it relied for its finding on what it had said about Periodic Reviews.

Contrary to the Panel's finding, the Appellate Body said zeroing in these Reviews violates Articles 2:4 and 9:5 of the *Antidumping Agreement*, and maintenance of the practice by the DOC ran afoul of these provisions.[111] It reviewed summarily its essential findings from Periodic Reviews and applied them to New Shipper Reviews, namely: both "dumping" and a "margin of dumping" relate to the pricing behavior of an exporter or foreign producer; dumping is determined, and a dumping margin calculated, for an exporter or foreign producer; negative comparison results (i.e., where Export Price exceeds Normal Value) may not be disregarded when calculating a dumping margin for an exporter; the dumping margin is the ceiling on the amount of AD duties that may be collected in respect of sales from an exporter or foreign producer; and if duties are paid by the importer and the ceiling is breached, then the importer may claim a refund.

Significantly, though, the Appellate Body did make clear zeroing in the context of both Periodic and New Shipper Reviews is unfair.[112] The violation of the mandate, in Article 2:4 of the *Antidumping Agreement*, to make a fair comparison, occurs because zeroing leads to the collection of AD duties in excess of the dumping margin – the ceiling. Without expressing it thusly, the Appellate Body implied (by relying on its previous explanations) the excess occurs because zeroing inflates the dumping margin, essentially creating not a metaphysical, but rather very real, distinction between: (1) the calculated but inflated margin associated with zeroing, on the one hand, and (2) the uncalculated but true margin without zeroing on the other.[113]

6. Zeroing in Sunset Reviews

Zeroing in Sunset Reviews was the fourth and final major topic on which the Appellate Body offered a finding. The Panel found no fault under Articles 2 and 11 of the *Antidumping Agreement* in

---

111. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 62(d), 139-42, 155-61, 181(d).

112. *See id.* ¶¶ 158-60.

113. The Appellate Body came close to articulating this distinction, during its discussion of zeroing as applied by the DOC in Period Reviews, when it wrote of an "exporters' *proper* margins of dumping." *Id.* ¶ 166.

respect of the American practice of zeroing in Sunset Reviews, nor in the two specific Sunset Reviews challenged by Japan. The Appellate Body reversed, finding zeroing both as such and as applied inconsistent with Article 11:3.[114]

What the DOC did in the Sunset Reviews is intriguing. In these Reviews, it is supposed to make a determination as to whether dumping would be likely to continue, or would be likely to recur, if the AD order at issue were lifted. This inquiry sometimes is called a "likelihood-of-dumping" determination. The DOC did not, in the Reviews, compute new dumping margins. Rather, the DOC relied on dumping margins it had established in prior proceedings, namely, Periodic Reviews, in which it had used Simple Zeroing.

The Appellate Body held that reliance by the DOC in Sunset Reviews on previous dumping margins calculated using zeroes was wrong under Article 11:3 of the *Antidumping Agreement*. Yet again, the Appellate Body turned to the expanding body of common law to which it had contributed. In *United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan*,[115] the Appellate Body said the text of Article 11:3, particularly the words "determine" and "review," require an authority to provide a "reasoned conclusion on the basis of information gathered

---

114. *Id.* ¶¶ 62(f), 169-78, 181(f). The Appellate Body exercised judicial economy and made no findings under Articles 2:1 and 2:4 of the *Antidumping Agreement*, nor under Articles V:1-2 of GATT. *See id.* ¶ 178.

Article 11:3 of the *Antidumping Agreement* says:

> Notwithstanding the provisions of paragraphs 1 and 2, any definitive anti-dumping duty shall be terminated on a date not later than five years from its imposition (or from the date of the most recent review under paragraph 2 if that review has covered both dumping and injury, or under this paragraph), unless the authorities determine, in a review initiated before that date on their own initiative or upon a duly substantiated request made by or on behalf of the domestic industry within a reasonable period of time prior to that date, that the expiry of the duty would be likely to lead to continuation or recurrence of dumping and injury. [The text contains a footnote here, stating: "When the amount of the anti-dumping duty is assessed on a retrospective basis, a finding in the most recent assessment proceeding under sub-paragraph 3.1 of Article 9 that no duty is to be levied shall not by itself require the authorities to terminate the definitive duty."] The duty may remain in force pending the outcome of such a review.

115. WT/DS244/AB/R (Dec. 15, 2003) [hereinafter *Corrosion-Resistant Steel*). This case is treated in our *WTO Case Review 2004*.

as part of a process of reconsideration and examination."[116] Any conclusion from a Sunset Review must be based on "reasoned and adequate conclusions" and be supported, both by "positive evidence" and a "sufficient factual basis."[117]

True enough, the precedent-setting case did not forbid zeroing in Sunset Reviews – the topic was not at issue. But, the Appellate Body did say in *Corrosion-Resistant Steel* that if an authority relies in a Sunset Review on dumping margins (*i.e.*, ones calculated before the Review) in making its likelihood determination, then it must be sure it calculated those margins in conformity with Article 2:4 of the *Antidumping Agreement*. If the margins were legally flawed because they were computed inconsistently with the Article 2:4 disciplines, then this defect "could give rise to an inconsistency not only with Article 2:4, but also with Article 11:3."[118] In turn, the likelihood-of-dumping determination "could not constitute a proper foundation for the continuation of anti-dumping duties under Article 11:3."[119]

Essentially, the Appellate Body recognized it had anticipated, consciously or not at the time, in *Corrosion-Resistant Steel,* the problem that arose in *Japan Zeroing*: an investigating authority might use – or better put, misuse – a prior defective dumping margin to justify continuation of an AD order. In *Japan Zeroing*, the Appellate Body needed only to connect two dots: (1) its statements in 2004 in *Corrosion-Resistant Steel* with (2) its findings in 2007 in *Japan Zeroing* that zeroing in Periodic and New Shipper Reviews was legally deficient under Articles 2:4 and 9:3. It did so with brevity and force. To rely on the previous margins, as the DOC did, was to misuse them.

7. Commentary

a. American Motives and Interests

The Appellate Body Report makes for persuasive reading. A more resounding defeat for the zeroing methodology and its advocates than rendered in the *Japan Zeroing* case is scarcely imaginable. The

---

116. *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 173 (quoting *Corrosion-Resistant Steel*, *supra* note 115, ¶ 111).

117. *Corrosion-Resistant Steel*, *supra* note 115, ¶ 114 (*quoting* the Panel Report in that case at ¶ 7.271), *quoted in Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 173.

118. *Japan Zeroing* Appellate Body Report, *supra* note 75, ¶ 174 (quoting *Corrosion-Resistant Steel*, *supra* note 115, ¶ 127).

119. *Id.* (quoting *Corrosion-Resistant Steel*, *supra* note 115, ¶ 130).

Appellate Body ruled against zeroing in original investigations. It ruled against zeroing in Sunset Reviews, Administrative Reviews, and New Shipper Reviews. In all these contexts, it ruled against both Model Zeroing and Simple Zeroing. The Appellate Body left open only a tiny crack for the lawful use of zeroing – to combat targeted dumping using the W-T methodology under Article 2:4:2 (second sentence). Consequently, the Appellate Body left open only one way for the advocates, few as they are among WTO Members, to resurrect zeroing, namely, through multilateral trade negotiations.

Only the most zealous of pro-zeroing advocates, perhaps, can read the *Japan Zeroing* Appellate Body Report – along with the considerable body of case law on the topic – and not speculate about American motives. At any rate, intentions that might lurk behind litigation positions resonate within law school classrooms and among hallway conversations. There is the possibility the United States defended zeroing to the last man, as it were, because of Congressional pressure exerted on the Executive Branch. It is also possible the Executive Branch knew its chances of success were low, but that a defeat would be an instrument to defuse Congressional pressure and encourage legislative change. Yet, why not point out to legislators charmed by zeroing that the methodology can fall into the wrong hands and be deployed against the long-term national economic interest?

Suppose the United States won the *Japan Zeroing* case, zeroing becomes lawful, and many other WTO Members adopt the methodology, following the lead of the DOC. Proliferation means American companies become victims of zeroing in foreign AD proceedings. Some companies may ship subject merchandise directly from the United States, and AD duties imposed by a foreign government will ultimately be detrimental to American workers making the goods within the scope of the foreign AD order. Other American enterprises may produce subject merchandise in a third country. A foreign AD order based on zeroing in the underlying dumping margin calculation would, at the very least, adversely affect the profitability of those companies, hurting share prices and thus investors, many of whom are Americans.

To be sure, not every member of the House of Representatives has both domestic producers facing import competition and exporters concerned about foreign trade remedy actions in his or her district. In addition, some Senators represent states dominated either by domestic producers or exporters. Legislators in those instances would reply that a pro-zeroing stance serves the interests of the majority of their business constituents (though not necessarily consumers). What this

stance does not serve, however, is the long-term national interest in boosting American exports and penetrating foreign markets.

b. Zeroing and the Doha Round

Unfortunately, some American Congressional officials have politicized the Appellate Body jurisprudence on zeroing.[120] In doing so, they risk detracting from the reputation and work of the Appellate Body. Reasonable minds can differ as to whether zeroing is, in a metaphysical sense, "fair" – just as they can differ as to what "fairness" is. No judicial opinion is flawless. But in every single zeroing case (and this *WTO Case Review* series has treated all of them), beginning in 2001 with *Bed Linen*,[121] the Appellate Body has been careful and considerate in reviewing substantive holdings in panel reports.

Lambasting the Appellate Body as judicially active and exceeding its standard of review under Article 17:6 of the *Antidumping Agreement* can be an expedient way to deal with decisions that a politician views, rightly or wrongly, as adverse to the short-term interests of favored constituents (notably, the Appellate Body expressly mentioned at the end of its *Japan Zeroing* decision that it was both mindful of and applying this standard[122]). Intimation that the Appellate Body reports are dim-witted can be an easy way to avoid expending many hours of hard study of those reports and eschew any effort to view them from different angles.

Nevertheless, the hostility of a minority group of United States Senators and Congressmen to the Appellate Body, or at least to its zeroing decisions, has been translated into an official American negotiating position in the Doha Round of multilateral trade negotiations. In turn, the November 2007 draft text on trade remedy rules circulated to WTO Members came close to adopting that position

---

120. The status of Doha Round negotiations, including on trade remedies and the positions and views of the United States and other WTO Members, is discussed and analyzed in Raj Bhala, *Doha Round Schisms – Numerous, Technical, and Deep*, 6 LOY. U. CHI. INT'L L. REV. (forthcoming fall/winter 2008).

121. *See* Appellate Body Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India*, WT/DS141/AB/R (Mar. 1, 2001).

122. *See Japan Zeroing* Appellate Body Report, *supra* note 75, ¶¶ 179-80.

on zeroing, though not on all other issues[123]. The text would forbid Model Zeroing in original investigations (a methodology the DOC ended in February 2007 anyway). But, reversing a number of Appellate Body decisions, the text would permit Simple Zeroing in original investigations and allow Simple or Model Zeroing in administrative, sunset, and new shipper reviews, and in the calculation of liability for (or refund of) AD duties. Not surprisingly, all other WTO Members oppose these textual proposals.

The point for now is that standing Appellate Body members cannot easily defend themselves or their work outside of what they write in reports. The United States needs courage to reduce the risk of detraction occurring to the reputation and work of the appellate body, an adjudicatory institution it championed in the Uruguay Round. But, in a context in which one party has little voice and some in the other party seem feckless, education about the Appellate Body and its zeroing reports, with the long-term in mind, is the casualty.[124]

---

123. Draft Consolidated Chair Texts of the AD and SCM Agreements, TN/RL/W/212, Nov. 30, 2007, art. 2.4.3, *available at* http://www.wto.org/english/tratop_e/rulesneg_e/rules_chair_text_nov07_e.htm.

124. It may be interesting to explore whether Article 17:4 of the WTO *Agreement on Antidumping* might play a role (or a higher profile one) in zeroing cases, and what the implications could be. Article 17:4 of the *Antidumping Agreement* states:

> If the Member that requested consultations considers that the consultations pursuant to paragraph 3 have failed to achieve a mutually agreed solution, and if final action has been taken by the administering authorities of the importing Member to levy definitive and anti-dumping duties or to accept price undertakings, it may refer the matter to the Dispute Settlement Body ("DSB"). When a provisional measure has a significant impact and the Member that requested consultations considers that the measure was taken contrary to the provisions of paragraph 1 of Article 7, that Member may also refer such matter to the DSB.

In turn, Article 7:1 provides:

> Provisional measures may be applied only if:
> (i) an investigation has been initiated in accordance with the provisions of Article 5, a public notice has been given to that effect and interested parties have been given adequate opportunities to submit information and make comments;
> (ii) a preliminary affirmative determination has been made of dumping and consequent injury to a domestic industry; and

B. Countervailing Duties

1. Citation

Japan – Countervailing Duties on Dynamic Random Access Memories from Korea, WT/DS336/AB/R, (issued November 28, 2007, adopted by the DSB on December 17, 2007) (complaint by Korea, with the EC and the United States as Third Participants).[125]

2. Introduction, Facts, and Panel Determinations

Japan – DRAMs is the third dispute over South Korea's alleged illegal subsidies of DRAMS manufactured by Hynix; the first two were brought to the DSB by the EC[126] and the United States.[127] In *US – DRAMs,* the United States fared better than Japan did in *Japan – DRAMs,* with the Appellate Body effectively confirming the respective subsidies determinations.[128] The panel results in *EC – DRAMs* were mixed, raising questions as to why the EC did not appeal, in reliance on *US – DRAMs.* Japan did not make the same error, but the differences in the investigations and findings were sufficiently great that the earlier Appellate Body decision did not carry the day.

(iii) the authorities concerned judge such measures necessary to prevent injury being caused during the investigation.

Arguably, a provisional AD duty levied on the basis of zeroing could have a significant impact on the home country of the exporter or foreign producer. That country could bring the matter to the WTO for dispute settlement.

125. Hereinafter Appellate Body Report, *Japan – DRAMS.*

126. Panel Report, *European Communities – Countervailing Measures on DRAM Chips,* WT/DS299/R (June 17, 2005), adopted Aug. 3, 2005 [hereinafter "*EC – DRAMS*"].

127. Appellate Body Report, *United States – Countervailing Duty Investigation on Dynamic Random Access Memory Semiconductors from Korea,* WT/DS296/AB/R (adopted July 20, 2005) [hereinafter *US – DRAMS* Appellate Body Report]; *see WTO Case Review 2005.*

128. *See US – DRAMS* Appellate Body Report, *supra* note 127, paras. 126, 192-93, 201, 204-07.

As many readers are no doubt aware, countervailing duty actions are governed by the WTO's *SCM Agreement.*[129] As a general rule, under the SCM Agreement government subsidies are actionable when they convey a benefit, are specific to an enterprise or industry and cause or threaten material injury.[130] In the present case, there was no serious doubt that any alleged benefits were specific, since they were afforded only to Hynix Semiconductor, Inc., a large Korean semiconductor manufacturer in difficult financial straits. However, whether a benefit was in fact conferred by government action was very much in dispute, as discussed below, as was whether the causation of injury requirement was met.

The Japanese investigating authorities ("JIA") had found no direct government subsidy provided to Hynix. The funds treated by JIA as subsidies to Hynix were actually provided by private creditors as part of a massive debt-restructuring program implemented in October 2001 and December 2002. However, direct payments are not required to establish an actionable subsidy under the SCM Agreement. Rather, it is sufficient if the government "entrusts or directs a private body," *inter alia,* to make financial contributions or direct transfers of funds (including loans) to the affected enterprise.[131] The JIA determined that certain aspects of the debt restructuring programs were countervailable subsidies, based on the "entrusts and directs" provision of the SCM Agreement, and a countervailing duty rate of 27.2% was imposed on DRAMs manufactured by Hynix and imported into the EU.[132]

Korea sought consultations and the formation of a panel in the DSU. The Panel found that the JIA's "entrustment" finding with regard to the loans provided to Hynix by four private creditors was erroneous with regard to a December 2002 restructuring, but agreed with the finding regarding an October 2001 bailout; the Panel's findings on benefit were similarly bifurcated. The Panel also found against JIA in several other respects, including the manner in which JIA had calculated the amount of the benefit (and thus the amount of the countervailing duties). The Panel further determined that the methodology used by JIA was not incorporated in Japan's countervailing duty legislation as required by the SCM Agreement and thus was not permitted. The Panel also found that Japan had imposed

---

129. *Agreement on Subsidies and Countervailing Measures,* Apr. 15, 1994, WTO Agreement, Annex 1A, *available at* http://www.wto.org/english/docs_e/legal_e/24-scm.doc [hereinafter SCM Agreement].

130. *Id.* at arts. 1, 2, 15.

131. SCM Agreement, *supra* note 129, art. 1.1(a)(1)(iv).

132. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶ 3.

countervailing duties on certain imports that had not been found to be subsidized. [133] Several procedural findings went against Korea, with the Panel affirming JIA's determination to force the private creditors to participate in the investigation as "interested parties" by providing requested data and then penalized them for not doing so. The Panel also effectively upheld JIA's causation of injury finding. [134]

3. Issues and Determinations on Appeal

Korea and Japan cross-appealed. Japan challenged the Panel's conclusions on JIA's "entrustment or direction" analysis, the existence of a benefit for Hynix, the calculation of the benefit, the alleged failure to include the calculation methodology in national legislation, and the application of duties to some unsubsidized imports.[135] Korea countered by challenging as error aspects of the Panel's decision that the October 2001 restructuring conferred a benefit on Hynix, that the creditors were properly joined as interested parties and that the restructurings had been a direct transfer of funds. It also challenged the consistency of WTO injury/causation analysis.[136] The Appellate Body addressed each of these issues in turn.

a. "Entrustment or Direction" by the Korean Government in December 2002

The Panel's finding of entrustment or direction, based on the standard noted above, had been based on creditor statements to the effect that the Korean Government had been directly involved in the restructuring and that it wanted Hynix to be saved, statements it felt were reasonably relied upon by JIA to support its entrustment or direction conclusion.[137] This was seen, logically enough, as evidence that the Korean Government influenced the creditors on behalf of Hynix. However, the Panel disagreed with the JIA's conclusion that the actions of the four creditors were not commercially reasonable, a conclusion on which the entrustment or direction finding depended.[138] For example, if a government agency provides loans to an enterprise at

133. *Id.* ¶ 7. Article 14 provides that any "method" used must be provided for in national legislation. SCM Agreement, *supra* note 129, art. 14.

134. Appellate Body Report *Japan – DRAMS*, *supra* note 125, ¶ 8.

135. *Id.* ¶ 116.

136. *Id.*

137. *Id.* ¶¶ 122-24.

138. *Id.* ¶ 127.

the same interest rates and other terms that would have been available from private banks – *i.e.*, at the market "benchmark" rate, there is no benefit conferred on the enterprise, and thus no subsidy.

Japan's principal concern was that the Panel effectively refused to permit JIA to rely on the totality of the evidence before it. Rather, the Panel had focused on the report of one of the four creditors to the exclusion of other evidence before JIA.

The Appellate Body first looked to its Report in *US – DRAMs*, noting that when the investigating authority relies, in its determination, on the totality of the evidence before it, the panel must consider "how the *interaction* of certain pieces of evidence may justify certain inferences that could not have been justified by a review of the individual pieces of evidence in isolation."[139] Here, JIA did not attach "decisive weight" to the issue of commercial reasonableness; this was not an intermediate finding that was central to the result. Instead, JIA made a "holistic assessment" of all the evidence before it. Under those circumstances, JIA was justified in concluding that the Korean Government intended to save Hynix in both restructurings and was prepared to make a direct intervention to that end.[140] Moreover, there may be entrustment or direction even if the loans made are commercially reasonable. Under the circumstances, according to the Appellate Body, the Panel failed to conduct the required objective assessment,[141] because it did not examine the evidence in its totality. This failure invalidated the Panel's finding that JIA did not properly determine entrustment or direction.[142]

b. JIA's Determination of Benefit

The JIA, like investigating authorities in other proceedings, determined the existence of a benefit to the recipient, in this case Hynix, largely by reference to the market – i.e., whether any funds provided by or through government action were provided on more favorable terms than would be available commercially. In the

---

139. *Id.* ¶ 131, *quoting US – DRAMs, supra* note 127, ¶ 157 (emphasis in original).

140. Appellate Body Report, *Japan – DRAMS, supra* note 125, ¶¶ 135-36.

141. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements . . . ." DSU, *supra* note 4, at art. 11.

142/ Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶¶ 139, 142.

investigation, JIA had found that the participation by the four creditor banks in the 2002 Hynix restructuring of debt was not commercially reasonable, and thus conferred a benefit under the SCM Agreement. In doing so, JIA effectively discounted a report prepared by one creditor, Deutsche Bank, which justified the lending on commercial grounds (*i.e.*, market-based rather than concessional), with JIA concluding that the report was not a sufficient basis to support the commercial reasonableness of the restructuring. JIA relied as well on press reports that impugned the commercial reliability of the Deutsche Bank Report.[143] Japan, before the Panel but after the JIA had made its determination, also relied on a consultant's report that further supported JIA's conclusion that the restructuring was not commercially reasonable.[144]

In this instance, the Appellate Body agreed with Korea that consideration of the consultant's report by the Panel was effectively an *ex post facto* justification for JIA's commercial reasonableness determination that had been properly rejected by the Panel. Consequently, the Appellate Body upheld the Panel's finding that JIA's determination of the existence of a benefit was inconsistent with the SCM Agreement.[145]

As to the October 2001 restructuring, the Panel agreed with JIA that the restructuring of debt conferred a benefit under the SCM Agreement, this time based on its conclusion that the four creditors had "failed to participate in the October 2001 [R]estructuring on the basis of commercial considerations."[146] Evidence that "other creditors" had also participated in the restructuring did not outweigh evidence that these four creditors had so acted,[147] as there was no evidence that those other creditors participated on the basis of commercial considerations either. (Such evidence would have suggested, contrary to JIA's existence of a benefit conclusion, that Hynix could obtain credit based on commercial considerations.)

The Appellate Body again decided that it was appropriate to apply a market-based analysis to determine the existence of a benefit. It noted that the JIA had no evidence before it suggesting that the non-entrusted and non-directed "other" creditors would have participated in the October 2001 restructuring on the same terms as did the relevant

---

143. *Id.* ¶¶ 148, 152.

144. *Id.* ¶ 159.

145. *Id.* ¶¶ 163-64.

146. *Id.* ¶¶ 216-18, (*quoting* Panel Report, *Japan – Countervailing Measures on Dynamic Random Access Memory Chips from Korea,* ¶ 7.275, WT/DS299/R (June 17, 2005) [hereinafter Panel Report, *Japan – DRAMs)*].

147. Panel Report, *Japan – DRAMS*, *supra*, note 146, ¶ 220.

four creditors. JIA had not had available to it any detailed data on the "other creditors," because none had responded to JIA's questionnaire. Under those circumstances, JIA had made an adverse inference, based on the lack of any evidence to the contrary,[148] that the other creditors had also participated in the October 2001 restructuring based on non-commercial considerations, and conferring a benefit on Hynix.[149] This approach, accepted by the Panel, was affirmed by the Appellate Body.[150]

c. Calculation of the Amount of Benefit

In its investigation, JIA had treated the debt-for-equity swaps used in the Hynix restructurings to be the equivalent of outright grants to Hynix, without considering any obligations that Hynix assumed to the creditors making the debt-equity swaps. In doing so, JIA relied on a "rational investor" standard, *i.e.*, what a rational market-driven investor would do in terms of accepting shares of stock in an enterprise that was bankrupt, arguably making the equity received in place of the unpaid debt valueless. Consequently, JIA treated the value of the Hynix equity provided to the creditors as zero.[151] Korea argued and the Panel agreed that the proper focus of the benefit analysis is on the net cost to creditors, rather than the net benefit to Hynix.[152]

The Appellate Body noted, "There is but one standard—the market standard— according to which rational investors act."[153] Article 14 of the SCM Agreement directs that equity infusions are not to be considered a benefit unless the decision is "inconsistent with the usual investment practice of private investors in the territory of that Member."[154] The Appellate Body faulted the Panel for making a distinction between "inside" and "outside" investors, a distinction the Appellate Body considered inappropriate.[155]

However, on the key issue, the Appellate Body agreed with the Panel that JIA did not sufficiently explain how it determined that from the point of view of Hynix that the value of the shares provided to the creditors was zero, given that both Hynix and the creditor banks

148. *See infra* part e.
149. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶ 228.
150. *Id.* ¶ 229.
151. *Id.* ¶¶ 166-67.
152. *Id.* ¶ 170.
153. *Id.* ¶ 172.
154. DSU, *supra* note 4, art. 14(a).
155. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶¶ 173-74.

treated the equity as having some value (even if less than the face value of the shares).[156] It thus affirmed the Panel's finding that JIA's analysis overstated the amount of the benefit conferred on Hynix[157] (which would have overstated the amount of countervailing duties ultimately assessed by Japan).

Korea also contended and the Panel determined that JIA had erred, in violation of the "national legislation" requirement of Article 14 of the SCM Agreement, by using a "method" to calculate benefit that was not "provided for in the national legislation or implementing regulations." The Appellate Body disagreed, essentially on the grounds that the "method" required to be set out in national legislation or regulations did not have to be set out in exhaustive detail, extending to the actual formulae applied by the investigating authority.[158] The Appellate Body also drew a distinction between the "method" for *calculating* the benefits and the methods used for *allocating* the benefits once the amount has been determined. Mathematical formulae used for the calculations are not "methods." The SCM Agreement does not require the allocation methodology to be set out in national legislation or regulations. Thus, the Panel erred by imposing that requirement.[159]

d. Allocation of Benefits – Non-Subsidized Exports

Korea alleged and the Panel agreed that Japan had imposed countervailing duties during 2006 on imports that JIA had found were not being subsidized at the time the subsidies were being imposed. The problem is not uncommon. Investigating authorities frequently amortize subsidies over a period of several years, rather than allocating the subsidy in its entirety to the year in which the benefit is actually received. In the instant case, JIA allocated a certain non-recurring subsidy over a five-year period (presumably reflecting the treatment of the funds under the 2001 restructuring program). While the five-year period ended before 2006, Japan nevertheless included that subsidy in the benefits, which were subject to countervailing duties beginning in 2006.[160]

---

156. *Id.* ¶¶ 176, 178. The creditors treated the equity at less than face value on their books, but still assigned a "substantial value" to it according to Korea.

157. *Id.* ¶ 182.

158. *Id.* ¶¶ 192-94.

159. *Id.* ¶¶ 201-02.

160. *Id.* ¶ 204.

The Appellate Body agreed with Korea and the Panel. It observed there is no requirement in Article 19.4 of the SCM Agreement[161] that the investigating authority conducts a new investigation to confirm the continued existence of the subsidies. However, when a non-recurring subsidy is identified and is determined by the investigating authority to be no longer in existence at the time the final determination to impose the countervailing duty is made, a countervailing duty cannot be imposed based on that particular subsidy.[162] According to the Appellate Body, the Panel was also justified in concluding that a non-recurring subsidy allocated over a five-year period beginning October 2001 would expire at the end of 2005[163] (allocated over 2001, 2002, 2003, 2004, and 2005), even though JIA did not so specify.

e. Involuntary Designation of "Interested Parties"

As noted in subpart b above, JIA had made certain adverse inferences because sixteen "other" Hynix creditors had refused to respond to JIA's questionnaires. Korea had challenged these determinations, *inter alia*, on the grounds that JIA had no authority to seek information from those creditors (and to draw adverse inferences from their failure to respond), because the creditors were not properly "interested parties" to the investigation. JIA made the determination based on "facts available."

Under the SCM Agreement, "In cases in which any interested Member or *interested party* refuses access to, or otherwise does not provide, necessary information within a reasonable period or significantly impedes the investigation, preliminary and final determinations, affirmative or negative, may be made on the basis of the *facts available*."[164] The doctrine exists largely because the investigating authority has no subpoena power or authority to compel either a foreign government or a company located in a foreign country to produce information that the investigating authority considers important to the investigation. The only leverage possessed by the investigating authority is the threat of adverse assumptions that would

161. SCM Agreement, *supra* note 129 ("No countervailing duty shall be levied on any imported product in excess of the amount of the subsidy found to exist, calculated in terms of subsidization per unit of the subsidized and exported product").

162. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶¶ 209-11.

163. *Id.* ¶¶ 214-15

164. SCM Agreement, *supra* note 129, art. 12.7 (emphasis added).

be harmful to the interests of the foreign producers being investigated or others affected by the proceeding.[165]

For purposes of the SCM Agreement, the term "interested party" includes the exporter, foreign producer or importer of the product subject to investigation, or a trade or business association the majority of the members of which are from one or more of those categories. The term also includes producers in the importing Member or associations the majority of which are producers.[166] However, "This list shall not preclude Members from *allowing* domestic or foreign parties other than those mentioned above to be included as interested parties."[167]

The essence of Korea's position was that JIA had improperly designated the sixteen non-responding "other" financial institutions as interested parties because those financial institutions had no interest in the outcome of the proceedings.[168] The Appellate Body agreed, but only in part. While the parties listed in the SCM Agreement have an interest in the outcome of the proceeding, the SCM Agreement does not indicate that those who may be designated "interested parties" are restricted to this listing. As the Appellate Body observed, "the mere fact that the lists . . . comprise entities that may be directly interested in the outcome of the investigation does not imply that parties that may have other forms of interest pertinent to the investigation are excluded."[169] The "allowing" language in the SCM Agreement noted above permitted the investigating authority, in the view of the Appellate Body (and of the Panel), to include, even to compel as interested parties, certain parties other than those explicitly listed. For the Appellate Body, this language thus expanded rather than restricted the investigating authority's power of inclusion.[170]

The Appellate Body explicitly recognized "differentiations in the nature of the interest that parties may have in participating in an investigation."[171] The investigating authority does not have "unfettered discretion" in designating interested parties; there must be some interest "related to the investigation," but not necessarily in the investigation's outcome. The investigating authority must also be mindful of the

---

165. This means that the affected producers and their government may try to pressure the recalcitrant interested party to provide requested data and otherwise cooperate in the investigation.

166. SCM Agreement, *supra* note 129, at arts. 12.9(i)-(ii).

167. *Id.* at art. 12.9 (emphasis added).

168. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶ 237.

169. *Id.* ¶ 238.

170. *Id.* ¶ 240.

171. *Id.* ¶ 242.

"burden" that designation may entail. Tellingly, the Appellate Body observes that "An investigating authority needs to have some discretion to include, as interested parties, entities that are relevant for carrying out an objective investigation and for obtaining information or evidence to relevant to the investigation at hand."[172]

Since, in this case, JIA was investigating allegations of entrustment or direction, it was reasonable for JIA, according to the Appellate Body, to seek information from Hynix's other creditors. If the other creditors had no interest in the outcome of the investigation, they should have provided JIA with information to that effect. [173] Consequently, according to the Appellate Body, JIA did not violate the SCM Agreement by including the other creditors as interested parties.[174]

f. Direct Transfer of Funds

Under the SCM Agreement, a subsidy is deemed to exist, *inter alia*, if "a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion) . . . ."[175] The question before the panel and the Appellate Body was whether the financial transactions undertaken with Hynix' October 2001 and December 2002 restructurings were "direct transfers of funds" under the SCM Agreement. Korea had asserted that this was not the case. In Korea's view, the referenced transactions simply changed the terms of existing claims and involved no provision of money to the subsidy recipient (Hynix). The Panel disagreed, accepting JIA's conclusion that the modification of the loan terms, through extending loan maturities and reducing interest rates on existing loans and converting unpaid interest to principal, along with debt-equity swaps, were properly characterized as "direct transfers of funds." [176]

The Appellate Body agreed and adopted a relatively broad definition of "funds," holding that the term encompasses "final resources and other financial claims more generally." In this respect the "e.g." in the phrase was significant; it suggests that the list, "grants, loans and equity extensions," is illustrative rather than exclusive.[177] If the financial position of the debtor was improved through debt

---

172. *Id.*
173. *Id.* ¶ 243.
174. Appellate Body Report, *Japan – DRAMS*, *supra* note 125,¶ 245.
175. SCM Agreement, *supra* note 129, at art. 1.1(a)(1)(i).
176. Appellate Body Report, *Japan – DRAMs*, *supra* note 125, ¶ 247.
177. *Id.* ¶¶ 250-51,

forgiveness, extension of payment periods, reduction of interest rates, or cancellation of debt through debt-equity swaps, this was properly treated by JIA as a "direct transfer of funds" under the SCM Agreement, Article 1.1(a)(1)(i), just as the Panel had determined.[178]

g. Causation of Injury

Article VI of the GATT provides that countervailing duties may not be imposed unless the effect of the subsidy "is such as to cause or threaten material injury to an established domestic industry, or is such as to retard materially the establishment of a domestic industry."[179] The SCM Agreement, Article 19.5, provides in pertinent part that "[i]f, after reasonable efforts have been made to complete consultations, a Member makes a final determination of the existence and amount of the subsidy and that, through the effects of the subsidy, *the subsidized imports are causing injury*, it may impose a countervailing duty in accordance with the provisions of this Article unless the subsidy or subsidies are withdrawn." Also, Article 15.5 of the SCM Agreement states that "[i]t must be demonstrated that the subsidized imports are, *through the effects of subsidies*, causing injury within the meaning of this Agreement."[180]

In this proceeding, Korea charged that it was insufficient for JIA to show simply that "the subsidized imports are causing injury." In addition, JIA should have shown that injury was caused "through the effects of subsidies."[181] The Panel and the Appellate Body both disagreed. Neither found any such additional requirement in Articles 15.5 and 19.5 The Appellate Body noted that, under 15.5, JIA was obliged to demonstrate a causal relationship between the subsidies and injury and to analyze the effects of the subsidized imports.[182] However, the relevant paragraphs of the SCM Agreement "neither envisage nor require the two distinct types of examinations suggested by Korea . . . ."[183] As further support, the Appellate Body noted that Article 11.2 of the SCM Agreement indicates that information related to volume and price effects of subsidized imports constitutes evidence "to demonstrate that injury is caused by the 'subsidized imports through the effects of

178. *Id.* ¶¶ 251-52, 256.

179. GATT, at art. VI(6).

180. Emphasis supplied in both provisions.

181. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶ 257.

182. *Id.* ¶¶ 262-63, (quoting from the SCM Agreement, *supra* note 129, arts. 15.2 and 15.4).

183. Appellate Body Report, *Japan – DRAMs, supra* note 125, ¶ 264.

subsidies.'"[184] It was thus sufficient for the investigating authority to carry out an examination demonstrating that the "subsidized imports are, through the effects of subsidies, causing injury" as set out in the SCM Agreement.[185]

4. Commentary

This is not a ground-breaking Appellate Body report, but it does provide useful guidance to investigating authorities in several instances – all situations in which their flexibility in conducting investigations is somewhat broadened, rather than narrowed by the Appellate Body.

a. Expanding the Definition of "Interested Parties"

While applying the concept of "interested parties" has commonly been subject to some discretion on the part of investigating authorities, this case confirms the relatively broad scope of this discretion. Significantly, an interested party does *not* need a direct interest in the outcome of the investigation. While it must have some form of interest, the Appellate Body effectively leaves the determination of that "other form of interest" to the investigating authority, unless or until the affected enterprise responds. What was effectively involuntary designation of certain financial entities as interested parties became an important tool for JIA in conducting its investigation. While these parties would not have been directly affected by the outcome of the investigation, they had access to information that was important to JIA, namely, whether there was a commercially reasonable basis for financial institutions to restructure the loans that had earlier been extended to Hynix.

If, as the Appellate Body ruled, JIA had discretion to treat the other creditors as interested parties, the ability of JIA and other investigating authorities in the future to conduct their investigations, and in this instance, to determine whether the loan restructuring constituted a benefit under the SCM Agreement, was greatly enhanced. In light of the Appellate Body's determination, JIA was effectively put in a "no lose" situation. If the other creditors had provided information that either confirmed that there was no commercial basis for the

184. *Id.* ¶ 270.
185. *Id.* ¶ 268.

restructuring, or suggested in contrast that such a basis existed, this would have facilitated JIA's ability to meet its responsibilities as investigating authority. Where the other creditors declined to do so, as here, JIA was entitled to draw adverse inferences, supporting its conclusion that a benefit was conferred by the four creditors' debt restructuring.

Does the decision in *Japan – DRAMs* mean that investigating authorities in the future will aggressively use designation of entities with possibly relevant information, but no significant connection, to the outcome of the investigations? Perhaps it does, but probably not on a regular basis. One can reasonably expect that in most instances the necessary "benchmark" information for determining whether a particular financial transaction confers a benefit under the SCM Agreement will be available from other sources.

Also, the Appellate Body has left open the possibility for an enterprise in the position of other creditors in *Japan – DRAMs* to avoid cooperating. The enterprise may explain to the investigating authority that the enterprise has no interest in the outcome of the investigation, or other interest in the proceedings. Alternatively, it may argue that, even if there is some interest, cooperation in the investigation would be unduly burdensome. In either instance, it may request that it not be treated as an interested party, and it will have a reasonable expectation that its status will be protected by the Appellate Body.

b. Defining "Funds" in the Context of "Direct Transfer"

A popular dictionary defines "funds" as "a sum or money or *other resources*."[186] While there is thus nothing radical in the Appellate Body's confirmation after a careful textual analysis of Article 1.1.(a)(1)(i) of the SCM Agreement that the term "funds" includes debt restructuring and debt-equity swaps, it confirms the willingness of the Appellate Body to accept a broader rather than narrower definition of what may constitute a subsidy. Because debt forgiveness improves the financial position of the borrower, it is equivalent to a direct transfer of funds. Similarly, debt-to-equity swaps, when "intended to address the deteriorating financial condition of the recipient company"[187] also amounts to a direct transfer of funds. In taking this approach, the

186. Merriam Webster On-Line, *available at* http://www.m-w.com/dictionary/funds.

187. Appellate Body Report, *Japan – DRAMs*, *supra* note 125, ¶ 252.

Appellate Body, following the lead of the Panel, addressed the substance of the transaction rather than simply the form and came to an economically sensible conclusion.

c. Splitting Hairs? – "Calculating" versus "Allocating"

In confirming that national legislation must set out the method used by the investigating authority to "calculate" the benefit, as required by Article 14.1 of the SCM Agreement, but not to "allocate" benefits, the Appellate Body again took a pragmatic approach to the requirements of the Agreement. For the Appellate Body, there is a limit to the level of detail that must be set out in national legislation, and this limit does not include mathematical formulae. It would make little sense, and impose considerable burdens on the investigating authority, if every aspect of the calculations had to be set out in national legislation. Among other things, it would make changes in allocation methodology difficult.

On the other hand, there is much to be said for transparency with regard to the methodology used by investigating authorities, whether that information is set out in statutes, regulations or operational manuals.[188] It would thus be unfortunate if this ruling by the Appellate Body is interpreted by investigating authorities as license to reduce the level of transparency in the processes used to allocate benefits in countervailing duty cases (or certain expenses in antidumping cases). Presumably, the Appellate Body will protect against that eventuality in future cases.

d. The Results – Who Won?

Neither Korea nor Japan was a clear winner or loser in *Japan – DRAMs*. While Japan and the JIA prevailed in most of the issues raised on appeal, JIA's determination that the December 2002 restructuring conferred a benefit, its calculation of the benefits for both restructurings and its imposition of countervailing duties based on non-recurring subsidies that had expired, were all faulted.[189] The question

---

188. *See, e.g.*, discussion of the U.S. "Sunset Policy Bulletin" in Appellate Body Report, *United States – Anti-Dumping Measures on Oil Country Tubular Goods (OCTG) from Mexico*, WT/DS282/AB/R (Nov. 2, 2005); *see WTO Case Review 2005*.

189. Appellate Body Report, *Japan – DRAMs*, *supra* note 125, ¶ 280.

thus arises as to how Japan will comply. At the meeting of the Dispute Settlement Body on January 15, 2008, Japan stated that it would implement the panel conclusions (presumably as modified by the Appellate Body) but would need a reasonable time to do so, and would consult with Korea on the matter. Korea suggested that implementation would simply require withdrawal of the notice imposing countervailing duties on DRAMs from Korea and urged Japan to do so without delay.[190] However, it seems very unlikely that Japan will simply throw in the towel. Rather, JIA is likely to modify its final determination in light of the Panel and Appellate Body reports and apply a recalculated, lower countervailing duty to Hynix exports to Japan.

190. WTO, WTO Members Adopt Dispute Panel Ruling on "Salmon," Jan. 15, 2008, *available at* http://www.wto.org/english/news_e/news08_e/dsb_15jan08_e.htm.