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# The Jurisprudence of the World Trade Organization in 2013

by Rachel Liechti, Tobias Naef & Tetyana Payosova<sup>1</sup>

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## I. Introduction

The year 2013 was less busy than previous years for WTO dispute settlement. WTO Members filed 20 notifications of “requests for consultations”, the Dispute Settlement Body (DSB) established twelve new dispute settlement panels, adopted three panel reports and one Appellate Body report.<sup>2</sup>

While few in number, the cases adjudicated in 2013 are of considerable importance. For the first time, a panel and the Appellate Body in *Canada – Feed-In Tariff Program*<sup>3</sup> ventured into the uncharted waters of trade in energy, in par-

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<sup>2</sup> All WTO Appellate Body Reports and panel reports are accessible online at <[www.wto.org](http://www.wto.org)>.

<sup>3</sup> Appellate Body report, *Canada – Measures Relating to the Feed-in Tariff Program*, adopted 24 May 2013, WT/DS426/AB/R; Panel report, *Canada – Measures Relating to the Feed-in Tariff Program*, WT/DS426/R.

ticular the legal status of renewable energy and measures of support to enhance its contribution to the energy mix. Secondly, the panel in *EC – Seal Products*<sup>4</sup> recognized that public morals of an importing country relating to processing products in the country of origin is a legitimate concern, which may restrict imports. It will be interesting to see how the Appellate Body rules on the point in 2014. It will be crucial in assessing so-called production and process methods (PPMs), which are also essential for environmental and human rights protection. It is noteworthy in the context of this report that both panels were chaired by Swiss nationals. Thirdly, the 2013 case law on anti-dumping, in the panel reports *China – X-Ray Equipment*<sup>5</sup> and *China – Broiler Products*,<sup>6</sup> had its focus on China, strengthening the rule of law in Chinese anti-dumping determinations and procedures.

## II. Subsidies in Canada: Feed-in Tariff Program

### A. Introduction and Facts

In 2009 Canada, following the example of several European countries including Germany, envisaged a feed-in tariff (FIT) scheme to promote investment in the development of its green energy industry. A FIT typically provides for a fixed price for “green” electricity – per kilowatt-hour (kWh) – fed into the grid for a certain period of time (long-term contracts are a common practice).<sup>7</sup> The province of Ontario went a step further and provided for a minimum domestic content requirement (DCR),<sup>8</sup> including a minimum percentage of renewable energy equipment originating from Ontario to be used by wind power and solar photovoltaic (PV) electricity generators in order to qualify for a FIT. Due to the DCRs in the province of Ontario, both Japan (on 13 September 2010) and the European Union (EU) (on 11 August 2011) brought a complaint against Canada to the WTO, as they felt their own producers of renewable energy equipment

<sup>4</sup> Panel report, *European Communities – Measures Prohibiting the Importation and Marketing of Seal Products*, appealed 24 January 2014, WT/DS401/R.

<sup>5</sup> Panel report, *China – Definitive Anti-Dumping Duties on X-Ray Security Inspection Equipment from the European Union*, adopted 4 April 2013, WT/DS425/R.

<sup>6</sup> Panel report, *China – Anti-Dumping and Countervailing Duty Measures on Broiler Products from the United States*, adopted 25 September 2013, WT/DS427/R.

<sup>7</sup> MIGUEL MENCONCA, DAVID JACOBS & BENJAMIN K. SOVACOO, *Powering the Green Economy. The Feed-in Tariff Handbook*, London 2010, pp. 15 ff.

<sup>8</sup> Minimum domestic content requirement is also often referred to as local content requirement (LCR).

were disadvantaged by this scheme.<sup>9</sup> The decision of the panel was subsequently appealed by all three parties to the initial dispute.

The FIT Program in the Province of Ontario was introduced in September 2009 according to the Direction of the Ontario Minister of Energy and Infrastructure by virtue of the amended Electricity Act 1998. This act defined a FIT Program as a programme for procurement of electricity, providing standard programme rules, standard contracts and standard pricing. The Minister of Energy in Ontario entrusted the Ontario Power Authority (OPA) with the task of establishing a FIT Program to procure electricity from all renewable sources except for hydropower through a 20-year power purchase agreement. The conditions of the FIT Program were detailed in FIT contracts – a power purchase agreement concluded between the OPA and the green electricity generators. The FIT Rules specified the parties' rights and obligations, identified relevant prices and provided an explanation of some of its key provisions, e.g. "Minimum Required Domestic Content Level" for qualifying solar PV and wind power generation facilities. The prices under the FIT Program were established by the OPA and intended to cover the development costs plus a reasonable rate of return (at the time of the dispute – 11 %) over the whole duration of a FIT contract. For "micro-generation projects" the microFIT contracts fulfilled the same role as the regular FIT contracts, and for solar PV generation facilities also included the minimum DCRs. The whole FIT Program pursued two fundamental objectives. First, it aimed to encourage new renewable energy generation facilities to participate in the Ontario electricity system and thus to diversify Ontario's supply-mix, to replace coal-fired plants, which were to be phased out by 2014, and to reduce greenhouse gas emissions. Secondly, the programme aimed to stimulate investment in the renewable energy generation equipment sector. The FIT scheme functioned as an exchange of performance obligations between the OPA and the green electricity suppliers (panel report, para. 7.216).

Both complainants, the EU and Japan, claimed that the Ontario FIT Program and its minimum DCR level as the condition of qualification for the programme is not compatible with the obligations of Canada under Art. 3.1(b) and 3.2 of the Agreement on Subsidies and Countervailing Measures (ASCM)<sup>10</sup> as it constitutes an import substitution subsidy, the Agreement on Trade Related Investment Measures (TRIMs Agreement)<sup>11</sup> and the General Agreement on

<sup>9</sup> WT/DS412/1, WT/DS/426/1 and WT/DS/426/1/Add.1 ; Third parties: Australia, Brazil, China, El Salvador, India, Korea, Mexico, Norway, Saudi Arabia, Chinese Taipei and United States.

<sup>10</sup> Agreement Establishing the World Trade Organization of 15 April 1994, Annex 1A, Agreement on Subsidies and Countervailing Measures (ASCM), SR 0.632.20.

<sup>11</sup> Agreement Establishing the World Trade Organization of 15 April 1994, Annex 1A, Agreement on Trade Related Investment Measures (TRIMs Agreement), SR 0.632.20.

Tariffs and Trade 1994 (GATT)<sup>12</sup> (panel report, paras. 7.72, 7.78). Canada argued in response that the FIT Program does not fall either under the TRIMs or under the GATT Art. III, as the whole scheme constitutes government procurement of electricity carried out through the OPA and thus falls under Art. III:8(a) (panel report, paras. 7.86–91). Moreover, Canada contended that this procurement is undertaken for governmental purposes and not with a view to commercial resale. Finally, to respond to the ASCM claims, Canada asserted that the FIT scheme can only be characterized as “purchase of goods by the government” under Art. 1.1(a)(1)(iii) ASCM and that the trade in electricity as an allegedly subsidized good is not affected (panel report, para. 7.185).

## **B. Findings**

The panel started its analysis with the determination as to whether the FIT Program constitutes an investment-related measure, and thus whether the TRIMs Agreement should apply. One of the key purposes of the FIT Program, as well as the FIT contracts, was to “encourage investment in the local production of equipment associated with renewable energy generation in the Province of Ontario” and it had indeed motivated some manufacturers (e.g. Siemens and ENERCON) to establish their renewable energy equipment production sites in Ontario (panel report, para. 7.109). Thus, the panel concluded that the TRIMs Agreement applies.

In its next step the panel clarified the relationship between Art. III:8(a) GATT and the TRIMs Agreement, namely whether the former can be applied as an exception both to Art. III:4 GATT and the TRIMs Agreement. There is an intrinsic link between GATT and the TRIMs Agreement, as the latter reiterates a national treatment obligation under Art. III GATT (Art. 2 TRIMs Agreement) and furthermore provides an illustrative list of those trade-related investment measures that are inconsistent with Art. III:4 GATT. Moreover, all the GATT exceptions apply to the TRIMs Agreement (Art. 3 TRIMs Agreement). The panel first resorted to paragraph 1(a) of the Illustrative List in the Annex to the TRIMs Agreement, which refers to a situation analogous to the case at hand, where, in order to receive an advantage, an enterprise has to purchase or use products of domestic origin. Thus, if the FIT Program were to be found inconsistent with Art. III:4 GATT and were to fall under any of the paragraphs of the Illustrative List, it would automatically be inconsistent with Art. 2.1 TRIMs (panel report, para. 7.117). This said, the panel noted that the FIT scheme could still be exempted from the scope of the national treatment

<sup>12</sup> General Agreement on Tariffs and Trade of 30 October 1947 (GATT), SR 0.632.21.

obligation by virtue of Art. III:8(a) GATT (panel report, para. 7.120). This understanding has been supported by the Appellate Body (Appellate Body report, para. 5.33).

The key question for the alleged national treatment violation remained whether the FIT Program was covered by Art. III:8(a) GATT. The panel established that the DCR of the FIT Program was a necessary prerequisite to qualify under the programme and thus was a “requirement governing the alleged procurement of electricity” (panel report, para. 7.128). Moreover, the panel explained that government “procurement” under Art. III:8(a) GATT shall be understood as “purchase” (obtaining possession/entitlement) of goods by a government in line with the interpretation under Art. 1.1(a)(1)(iii) ASCM. Finally, it addressed the question of whether the given sale “is for governmental purposes and not with the view to commercial resale or with a view to use in the production of goods for commercial resale”. Canada opined that “governmental purposes” are to be interpreted more broadly than “for governmental consumption”, as it is a requirement separate from “not for commercial resale”. However, the panel did not support this approach (panel report, para. 7.141). It found that Art. III:8(a) GATT should be read in the context of Art. XVII:2 GATT dealing with similar situations for state-trading enterprises. This confirms that “not for commercial resale” forms part of “governmental purposes”. Thus, in the case that the purchase of electricity under the FIT Program is undertaken “with a view to commercial resale” it does not fall under the government procurement exemption of Art. III:8(a) GATT. The Appellate Body disagreed with the panel on this point. It found that the very wording of Art. III:8(a) GATT suggests that the requirements of “governmental purpose” and of “not for commercial resale” are cumulative. Furthermore, the Appellate Body found that “commercial resale” has to be assessed with due regard to the entire transaction, including the long-term strategy of the seller as well as the buyer’s perspective. It confirmed that Art. III:8(a) GATT refers to the situation where goods are purchased for the use of the government, consumed by government, or provided by government to recipients in the discharge of its public function (Appellate Body report, para. 5.74).

The electricity market model employed in the Province of Ontario led the panel to find that the Government of Ontario, through its agencies, namely the OPA and indirectly also the Independent Electricity System Operator, and the local distribution companies, was purchasing electricity under the FIT and microFIT contracts. This electricity was then injected into the grid through transmission and distribution networks and only then sold to the final consumer. The electricity produced under the FIT Program and purchased by the OPA was consumed through the same channels and thus resold to private consumers in competition with other private-sector electricity retailers. However, Canada



disagreed with this interpretation, as it held that there was no electricity market in Ontario where classically “supply and demand freely meet” (panel report, paras. 7.147–8). The panel, however, clearly stated that it is not decisive whether the OPA makes any profits from the sales of electricity. The electricity transmission and distribution companies, i.e. Hydro One, which is fully owned and controlled by the Government of Ontario, and local distribution companies which are up to 94% owned by municipal governments, were selling electricity on a profit-seeking basis. Thus, the government of Ontario benefited from the operations (panel report, para. 7.150). For these reasons, the panel found that Canada cannot invoke Art. III:8(a) GATT, as the government procurement of electricity in Ontario was undertaken with a view to commercial resale. The Appellate Body upheld the overall finding of the panel on Art. III:8(a), however, discerned on the reasoning. The Appellate Body strongly emphasized that the government procures electricity, whereas the product that is arguably treated less favourably is different – namely, the generation equipment – which is purchased directly by the generators. While the panel recognized these differences between the products, it found that a close relationship between the electricity and the generation equipment is sufficient for electricity procurement to fall under Art. III:8 GATT. The Appellate Body disagreed on this point. It concluded that electricity and generation equipment are not in a competitive relationship and thus procurement of electricity does not fall within the scope of Art. III:8 GATT (Appellate Body report, paras 5.75–9).

After a thorough analysis of the FIT Program the panel found that a minimum “required domestic content level” is a necessary prerequisite to participating in the programme and to receiving advantages in the form of a guaranteed price for electricity for a period of 20 years. Therefore, the panel concluded that the FIT Program by virtue of its local content requirement (LCR) falls under para. 1(a) of the TRIMs Illustrative List, and thus in light of Art. 2.2 TRIMs Agreements is inconsistent with Art. III:4 GATT and Art. 2.1 TRIMs Agreement (panel report, paras. 7.165, 7.167).

Following the assessment under GATT, a challenging task before the panel was to determine whether the FIT Program constitutes a subsidy within the meaning of the ASCM and GATT. First the panel had to determine in which form the subsidy exists in the present case. Japan claimed that the Ontario feed-in tariff constitutes a financial contribution in the form of a “direct transfer of funds” or a “potential direct transfer of funds” as it is similar to a conditional grant, or alternatively an “income or price support” in the sense of Art. XVI GATT (panel report, para. 7.169). In addition to the argument put forward by Japan, the EU also argued that a feed-in tariff alternatively constitutes a financial contribution that was provided under the entrustment of a private company (local distribution companies) by the government of Ontario. Furthermore, in

an alternative the EU considered that the feed-in tariff can amount to a financial contribution through a “purchase of goods” within the meaning of Art. 1.1(a)(1) (iii) of the ASCM Agreement. Canada, on the other hand, clearly understood its feed-in tariff scheme as a “purchase of goods”, i.e. purchase of electricity by the OPA acting as an agent of the Government of Ontario. The panel found that the FIT Program does indeed constitute a “government purchase of goods” as there is an “exchange of rights and obligations including a payment of money” and thus cannot constitute other forms of financial contribution (panel report, para. 105).<sup>13</sup> While the Appellate Body disagreed on the fact that a FIT Program cannot simultaneously fall under more than one form of financial contribution, it concurred with the panel’s findings under Art. 1.1(a)(1) ASCM (Appellate Body Report, para. 5.121).

In order to establish that the Ontario FIT Program in law constitutes a subsidy, the panel had to turn to the analysis of the “benefit” potentially conferred by the purchase of electricity through OPA. Japan, as well as the EU, contended that both FIT and microFIT contracts guaranteed a higher price for electricity than the price available on the wholesale and/or retail markets in Ontario, and also in other provinces of Canada. The EU also noted the 20-year duration of these contracts and thus of the privileged pricing for qualifying facilities. Both Japan and the EU agreed on the point that without the FIT Program, renewable energy generation facilities, which are less-cost efficient than the existing mainly fossil-fuel generation facilities, could not have survived on the market of Ontario but for the existence of the FIT scheme. Interestingly, unlike Japan, the EU suggested that the benchmark for benefit determination should reflect the differences between various generation technologies (renewable vs. fossil fuel). Here, according to the EU, the panel should have compared various types of renewable energy (e.g. biomass vs. solar PV), which according to the FIT Program have indeed been treated differently. The EU also alleged that the FIT prices were standardized and thus were not adjusted to the actual cost of green electricity production, thus inevitably resulting in benefit. Canada in its turn submitted that none of the proposed benchmarks was appropriate (panel report, paras. 7.250–63).

The panel continued its analysis under “benefit” requirement by referring to Art. 14 ASCM as a context for interpretation.<sup>14</sup> Following established WTO practice, the existence of an advantage provided through a financial contribution has to be assessed not in the abstract, but in comparison to the market-

<sup>13</sup> See also in this sense, Appellate Body report, *United States – Measures Affecting Trade in Large Civil Aircraft – Second Complaint*, adopted 23 March 2012, WT/DS353/AB/R, para. 619.

<sup>14</sup> Appellate Body report, *Canada – Measures Affecting the Export of Civilian Aircraft*, adopted 4 August 2000, WT/DS70/AB/R (*Canada–Aircraft*), paras. 155 and 158.

place.<sup>15</sup> Art. 14 ASCM clarifies that where a government purchases goods the advantage would exist only where remuneration for those goods was more than adequate compared to the prevailing market conditions (panel report, para. 7.271). Previous WTO jurisprudence also clarified that for the purpose of Art. 14 ASCM in cases where a market is the main object of government intervention, it cannot serve as an appropriate benchmark to determine a benefit (panel report, para. 7.274). The panel in turn addressed the arguments of the complainants, which suggested that the wholesale electricity market in Ontario, or in four other out-of-province jurisdictions, should serve as a benchmark. The panel disagreed on both points. It characterized the electricity wholesale market of Ontario as a part of Ontario's electricity system. This system is closely regulated by the Government of Ontario in order to achieve the envisaged electricity supply mix in the province and which is needed to ensure long-term security of supply. Also, according to the panel, the out-of-province markets do not satisfy the current needs of the market in Ontario and thus cannot reasonably serve as a benchmark. Moreover, the panel underlined that the very nature of the modern electricity system is that governments determine the proper energy mix. Finally, the panel suggested that it could see that it might be possible to determine a benefit by comparing the rate of return obtained by the FIT generators under the FIT and microFIT contracts (set at 11%) with the "average cost of capital in Canada for projects having a comparable risk profile in the same period". However, due to the lack of evidence on the record the panel could not complete this analysis (panel report, para. 7.326). In conclusion, the panel did not find whether a FIT Program constituted a subsidy or not.

The complexity of the benefit analysis was also reflected in the fact that one of the panellists disagreed with the decision of the panel on this very point (panel report, paras. 9.1–23). The dissenting panellist suggested that prices on the out-of-province markets can serve as a benchmark if these markets are not as heavily distorted by government intervention as in Ontario, and where these prices were adjusted to the prevailing market conditions in Ontario. However, again sufficient information to make conclusive findings was unavailable.

The Appellate Body disagreed with the panel on determination of a relevant market, as the latter suggested that the electricity market as a whole should be

<sup>15</sup> Appellate Body Report, *Canada – Aircraft*, para. 157; Panel Report, *United States – Tax Treatment for "Foreign Sales Corporations"*, adopted 20 March 2000 as modified by the Appellate Body report, WT/DS108/R (*US – FSC*), para. 7.103; Appellate Body report, *US – FSC*, adopted 20 March 2000, WT/DS108/R, para. 140; Panel report, *US – FSC (Article 21.5 – EC)*, adopted on 29 January 2002 as upheld by the Appellate Body report, WT/DS108/RW, paras. 8.44–8; Appellate Body report, *US – FSC (Article 21.5 – EC)*, adopted on 29 January 2002, WT/DS108/AB/RW, para. 198.

considered, whereas the former noted that, based on a more detailed analysis of demand-side as well as supply-side factors, first and foremost the cost structures and operating costs in light of the intermittent nature of renewable energy sources and the energy mix determined by the government, it is possible to differentiate the market for renewable energy.<sup>16</sup> Moreover, the Appellate Body emphasized that government interventions to create a market cannot at the same time distort this market, as it comes into existence only because of governmental policies. Thus, the question to be asked in this regard is whether the market already existed at the time of governmental intervention (Appellate Body report, para. 5.188). Accordingly, a benchmark for the benefit analysis should have also been chosen based on the energy mix determined by the Government of Ontario, i.e. the prices for the wind power- and solar PV-generated electricity set during the competitive bidding process. For this reason, the Appellate Body reversed the findings of the panel, however it could not complete the analysis itself due to lack of evidence on record (Appellate Body report, para. 5.245).

### C. Commentary

This case is an important development of the WTO jurisprudence in light of internationally widespread measures targeted at promotion of renewable energy. It is the first case in the WTO which explicitly deals with a very specific energy sector, namely electricity.<sup>17</sup> The panel recognized that electricity constitutes a good, thus leaving no doubt that electricity falls within the scope of the WTO law and its disciplines on trade in goods. Notably, both the panel and the Appellate Body resorted to a very profound analysis of the local Ontario electricity system and its electricity market, taking into consideration not only the specific nature of electricity, but also the economics of electricity markets and government choices as to the energy mix. Importantly, the panel explicitly recognized the role of governments in securing a safe, reliable and sustainable supply of electricity for the long term (panel report, para. 7.284). In this light, both the panel and the Appellate Body, although from different perspectives, recognized the regulatory space of governments in determining the energy mix, as a way to address negative and positive externalities associated with electricity production from both conventional and renewable sources. Finally,

<sup>16</sup> On demand-side and supply-side considerations see also: Appellate Body report, *European Communities – Measures Affecting Trade in Large Civil Aircraft*, adopted 1 June 2011, WT/DS316/AB/R, para. 1121.

<sup>17</sup> Only a few previous cases were related to the energy sector, e.g. *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2.

such governmental policies can be seen to reflect “consumers’ readiness to purchase electricity from a combination of different electricity generation technologies”.

While renewable energy has in some instances already achieved competitiveness with fossil fuels,<sup>18</sup> its initial integration into the energy market always requires considerable governmental support, both in the form of determination of the energy mix and financial contributions. Thus most countries worldwide, including Switzerland, are still supporting their renewable energy generation sector and seem to mutually tolerate these policies. This viewpoint is also confirmed by the fact that, in the present case, neither Japan nor the EU challenged the FIT scheme itself. However, the change in current policies (e.g. phase-out of FITs) may lead to decreased tolerance of such schemes. The question that remains is whether FITs as such are compatible with the WTO law. It is important to note that the current panel and the Appellate Body had to deal with a specific system and the emphasis of the case was on LCRs of the system. They were limited by the terms of reference and did not engage either in the analysis of specificity or of adverse effects, that would otherwise be crucial for a determination of an actionable subsidy. On the other hand, the WTO adjudicating bodies clearly outlawed the LCRs in the renewable energy sector. However, there is an ongoing academic debate as to whether, in certain instances, LCRs should be allowed in the future e.g. through the introduction of new rules.<sup>19</sup> For some years, concerns have been expressed as to the lack of disciplines that would allow subsidies for green energy promotion even without LCRs, especially due to the phase-out of the non-actionable subsidies under Art. 8 ASCM, and suggestions have been put forward to amend the existing WTO law.<sup>20</sup> Relevant work in academic circles is currently in progress.<sup>21</sup>

Finally, this case is also important because it emphasizes the differences between energy markets even within the same country, thus suggesting that in similar cases the exact analysis will to a large extent depend on specific features

<sup>18</sup> TIM KEATING, *Death to PV Subsidies*, Renewable Energy World, available at: <<http://bit.ly/1hZd2DF>> (9 April 2014).

<sup>19</sup> JAN-CHRISTOPH KUNTZE & TOM MOERENHOUT, *Local Content Requirements and the Renewable Energy Industry – A Good Match?*, May 2013, International Centre for Trade and Sustainable Development, Geneva, Switzerland, online at <[www.ictsd.org](http://www.ictsd.org)> (9 April 2014); SHERRY M. STEPHENSON, *Addressing local content requirement: Current challenges and future opportunities*, July 2013, International Centre for Trade and Sustainable Development, Geneva, Switzerland, online at <[www.ictsd.org](http://www.ictsd.org)> (9 April 2014).

<sup>20</sup> JAMES BACCHUS, *World Trade Rules need an Exemption for Green Energy*, *International Business Times*, 2 November 2012.

<sup>21</sup> See e.g.: Work Package 5 on Trade and Climate Change of the NCCR Trade Regulation (WTI), E-15 Expert Group on Clean Energy Technologies and Sustainable Energy Trade Initiative (ICTSD), Forum on Trade and Green Economy (UNCTAD) and Global Subsidies Initiative (IISD).

of the electricity market concerned. The most recent WTO case, consultations on which were initiated for the second time in February 2014 by the US against India on its National Solar Mission<sup>22</sup> might contribute valuable findings and will be addressed in due course in future SZIER issues.

### **III. Technical Barriers to Trade in the EU: *EC – Seal Products***

#### **A. Introduction and Facts**

On 16 September 2009 the European Union adopted a regulation which only allows the placing of seal products on the EU market where they “result from hunts traditionally conducted by Inuit and other indigenous communities and contribute to their subsistence”.<sup>23</sup> Moreover, two derogations were made from the main principle, which allow the import of seal products, (i) where they are imported for the personal use of travellers and their families and (ii) where they result from products of “hunting that is regulated by national law and conducted for the sole purpose of the sustainable management of marine resources”.<sup>24</sup>

The main objective stated in the regulation is the welfare of seals as “sentient beings that can experience pain, distress, fear and other forms of suffering”.<sup>25</sup> As the hunting of seals had led to “expressions of serious concern by members of the public and governments sensitive to animal welfare considerations” some, but not all, Member States of the EU had adopted or planned legislation regulating trade in seal products.<sup>26</sup> Therefore, another aim of the regulation is to “harmonise the rules across the Community [...] and thereby prevent the disturbance of the internal market in the products concerned”.<sup>27</sup> Nonetheless, the EU was convinced that the “fundamental economic and social interests of Inuit communities engaged in the hunting of seals as a means to ensure their subsistence should not be adversely affected”.<sup>28</sup> The regulation provides for the

<sup>22</sup> Request for consultations by the United States, *India – Certain Measures Relating to Solar Cells and Solar Modules*, Addendum, WT/DS456/1/Add, 11 February 2014.

<sup>23</sup> Regulation (EC) 1007/2009 of the European Parliament and the Council of 16 September 2009 on trade in seal products, 2009 OJ L 286/26, hereafter EU Regulation, Art. 3 para. 1.

<sup>24</sup> EU Regulation, Art. 3. para. 2.

<sup>25</sup> *Ibid.* Preamble, para. 1.

<sup>26</sup> *Ibid.* paras. 4 and 5.

<sup>27</sup> *Ibid.* para. 8.

<sup>28</sup> *Ibid.* para. 14.

EU Commission to be empowered to set out specific requirements for the three exceptions in a separate implementing regulation.<sup>29</sup>

Norway and Canada claimed that the EU Regulation(s) – either the implementing measure in itself or in combination with the basic regulation – violate(s) various obligations of the EU under the GATT 1994 and the TBT Agreement.<sup>30</sup> After unfruitful consultations with the EU, they requested the establishment of a WTO Panel to decide on the obligations and the relationship between the GATT 1994 and the TBT Agreement.<sup>31</sup> The panel made its decision and circulated its report to Members on 25 November 2013. The findings were appealed and the report of the Appellate Body is expected in 2014.

## B. Findings

First of all, for a proper common understanding, the panel had to legally characterize the measure(s) at issue. It concluded that the basic EU regulation, although it nowhere uses words such as “ban” or “prohibit”, but rather “only” allows the placing on the market of certain seal products, it effectively operates as a ban on seal products which do not meet the conditions under the measure. Therefore the EU Seal regime, in its entirety, consists of a ban, combined with one exception – the Inuit exception (IC exception) – and two derogations; (i) the traveller’s exception and (ii) the marine resource management exception (MRM exception). The commission regulation,<sup>32</sup> which lays down detailed rules on the implementation of the basic regulation, constitutes a part of the regime (panel report, para. 7.2.2).

As claims had been made that obligations, mainly under the GATT and the TBT Agreement, had been violated, the panel decided in a second step on the order of its analysis. Following the guidance of the Appellate Body<sup>33</sup> and the

<sup>29</sup> *Ibid.* para. 17.

<sup>30</sup> Agreement Establishing the World Trade Organization of 15 April 1994, Annex 1A, Agreement on Technical Barriers to Trade (TBT Agreement), SR 0.632.20. This contribution will only deal with the main substantial claims of discrimination and trade restrictiveness and not with the procedural claims.

<sup>31</sup> For a summary of the consultations and proceedings see online at <<http://bit.ly/1a4AYFU>> (9 April 2014).

<sup>32</sup> Commission Regulation (EU) 737/2010 of 10 August 2010 laying down detailed rules for the implementation of Regulation (EC) 1007/2009 of the European Parliament and of the Council on trade in seal products (implementing regulation).

<sup>33</sup> Appellate Body reports, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, adopted 25 September 1997, WT/DS27/AB/R (*EC – Bananas III*) and *European Communities – Trade Description of Sardines*, adopted 23 October 2002, WT/DS231/AB/R (*EC – Sardines*).

three latest panels dealing with TBT issues,<sup>34</sup> it concluded that, if the measure at issue were a “technical regulation”, it would then be appropriate to begin the analysis with the claims under the TBT Agreement, followed by those under GATT (para. 7.2.3).

The TBT Agreement defines the term “technical regulation” as a document, which lays down product characteristics or their related PPMs, including applicable administrative provisions, with which compliance is mandatory (Annex 1.1 TBT Agreement). This document may also include terminology, symbols, packaging, marking or labelling requirements applicable to a product or a PPM. Deriving from the wording of this definition, the Appellate Body has developed a three-tier test to examine whether a document can be qualified as a “technical regulation”:

*“First, the document must apply to an identifiable product or group of products. The identifiable product or group of products need not, however, be expressly identified in the document. Second, the document must lay down one or more characteristics of the product. These product characteristics may be intrinsic, or they may be related to the product. They may be prescribed or imposed in either a positive or a negative form. Third, compliance with the product characteristics must be mandatory.”*<sup>35</sup>

Based on the analysis of these three criteria the panel determined that the EU Seal regime constituted a technical regulation (para. 7.125) and continued to consider the claim under Art. 2.1 TBT. The article provides that Members must not treat imported products from any Member less favourably than like products of national origin and like products originating in any other country. These are the so-called obligations of “national treatment” and “most-favoured nation treatment”.<sup>36</sup>

The panel held that the IC exception violated the obligations of national and most-favoured nation treatment (paras. 7.319 and 7.353). It argued that seal products which are prohibited and seal products which are allowed under the

<sup>34</sup> Panel reports, *United States – Measures Affecting the Production and Sale of Clove Cigarettes*, adopted 24 April 2012 as modified by the Appellate Body report, WT/DS406/R (*US – Clove Cigarettes*); *US – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products*, adopted 13 June as modified by the Appellate Body report, WT/DS381/R (*US – Tuna II (Mexico)*) and *US – Certain Countries of Origin Labelling (COOL) Requirements*, adopted 23 July 2012 as modified by the Appellate Body report, WT/DS384/R (*US – COOL*).

<sup>35</sup> Appellate Body report, *EC – Sardines*, para.176, summarizing the Appellate Body’s interpretation in *European Communities – Measures Affecting Asbestos and Products Containing Asbestos*, adopted 5 April 2011, WT/DS135/AB/R (*EC – Asbestos*), paras. 66–70.

<sup>36</sup> See THOMAS COTTIER & MATTHIAS OESCH, *International Trade Regulation. Law and Policy in the WTO, the European Union and Switzerland*, Berne/London 2005, pp. 346–427 for a detailed analysis of these two principles in WTO law.



EU Seal regime are like products (para. 7.3.2.1) and that the regime has a “detrimental impact on the competitive opportunities of Canadian imported products vis-à-vis Greenlandic imported and EU domestic products” (panel report, para. 7.170). It continued that although the distinction between commercial and IC hunts was justifiable, based on the purpose of the hunt, it was not “designed and applied in an even-handed manner”. As the EU had failed to demonstrate that the detrimental impact stemmed exclusively from a legitimate distinction, the IC exception in the regime was therefore found to be inconsistent with the EU’s obligations under Art. 2.1 TBT (para. 7.319). The same was found for the MRM exception (para. 7.353).

Art. 2.2 TBT provides that Members must not prepare, adopt or apply technical regulations with a view to or with the effect of creating unnecessary obstacles to international trade. The article further rules that technical regulations must not be more trade-restrictive than necessary to fulfil a legitimate policy objective, taking into account the risks which would be created by non-fulfilment. To assess whether a measure is consistent with this article, a panel first has to identify the objective and subsequently analyse whether the particular objective is legitimate. To ascertain whether a measure is necessary:

*“[a] panel should begin by considering factors that include: (i) the degree of contribution made by the measure to the legitimate objective at issue; (ii) the trade-restrictiveness of the measure; and (iii) the nature of the risks at issue and the gravity of consequences that would arise from non-fulfilment of the objective(s) pursued by the Member through the measure. In most cases, a comparison of the challenged measure and possible alternative measures should be undertaken.” (Para. 7.355 citing Appellate Body report, US-Tuna II (Mexico), paras. 312–22)*

An examination of the EU Seal regime shows that its objective is public moral concerns regarding the “incidence of inhumane killing of seals”, an objective which falls within the scope of legitimate measures within the meaning of Art. 2.2 TBT because “the concept of public morals is a relative term which needs to be defined based on the standard of right or wrong in a given society” (Para.7.411–21). The panel goes on to confirm a certain degree of the regime’s actual contribution in addressing public moral concerns on seal welfare, although the contribution is diminished by the three exceptions, and the level of protection actually achieved by the measure is most likely not as high as the EU initially expected (paras. 7.441–66).

Canada and Norway had proposed a regime with animal welfare requirements for seal hunts and certification of conformity combined with labelling requirements as an alternative, less trade-restrictive measure than the ban (para. 7.468). The panel however rejected the proposal, explaining that such a certification system would need to be able to distinguish between seals killed

in accordance with the relevant requirements, and those killed inhumanely, in order to ensure that public moral concerns on animal welfare were actually being addressed. Such a system could however “impose large costs and/or logistical demands on those participating in the hunt and subsequent marketing of products” (para. 7.497) and therefore be regarded as being less reasonably available taking into account the risks non-fulfilment would create (paras. 7.499–505).

The panel also observed a violation of the EU’s national treatment and most-favoured nation treatment obligations under the GATT Agreement<sup>37</sup> – for the same reasons as under the TBT Agreement – by the less favourable treatment of imported products outside the scope of the foreseen exceptions (paras. 7.4.2 and 7.4.3).

Art. XX of the GATT provides for general exceptions – or legitimate policy goals – *inter alia* to the basic rule in Art. XI, which forbids the introduction of quantitative import and export restrictions and measures having the same effect.<sup>38</sup> According to Art. XX, measures which are necessary to protect public morals (lit. a) or animal health (lit. b) are – among others – allowed to be adopted and enforced by Members, as long as they 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”.

Building on its argumentation under the TBT Agreement, the panel found that the EU Seal regime can be “provisionally deemed necessary within the meaning of Art. XX(a)” (paras. 7.630–39) before examining its consistency with the other requirements of the provision – the so-called chapeau. Here again, it referred to its analysis under the TBT Agreement and reiterated that due to the lack of even-handedness in the design and the application of the IC and the MRM exceptions, these were not consistent with the requirements of the chapeau in Art. XX (paras. 7.630–39). It found, moreover, that the EU had failed to establish a *prima facie* case under Art. XX(b) (para. 7.640).

## C. Commentary

In January 2014, Canada, Norway and the European Union notified the WTO dispute settlement body of their decisions to appeal certain issues to the Appellate Body.<sup>39</sup> Independent of the Appellate Body’s decision in the matter, there

<sup>37</sup> In Art. I:1 and III:4.

<sup>38</sup> See COTTIER & OESCH, *supra* n. 36, pp. 428–512 for a detailed analysis of these general exceptions, or rather legitimate policy goals, in WTO law.

<sup>39</sup> For the current status of the dispute see online at <<http://bit.ly/1hvjft>> (9 April 2014).

are various points of interest where the panel has been challenged by this dispute. For the first time in history a WTO panel deemed a measure necessary to protect public moral concerns under GATT Art. XX(a) and TBT Art. 1, although the exception had been invoked twice before in earlier cases, once under GATT and once under the General Agreement on Trade in Services (GATS).<sup>40</sup>

On the one hand, the examination of the necessity test includes weighting the importance of the policy objective in relation to the trade-restrictive impact of the measure at stake. On the other hand, it has not yet been authoritatively decided by the Appellate Body whether and under what circumstances the public morals exception can serve to justify measures which pursue “extraterritorial” objectives, such as the welfare of animals living in another Member of the WTO. By identifying the objective of the EU Seal regime as “addressing EU public moral concerns on seal welfare”, (paras. 7.415, 7.631) the panel demonstrated that it primarily aimed at protecting moral concerns within the EU, and only secondly the welfare of seals outside the EU. Thus the exception was found to be justified.<sup>41</sup>

In June 2011, Oskar Freysinger, member of the Swiss National Council, submitted a motion to ban seal products in Switzerland in the same way as in the EU.<sup>42</sup> In the meantime, however, the ordinance on the declaration on fur and fur products has come into force, introducing an obligation to declare furs and pelts when offered for sale in Switzerland.<sup>43</sup> The Swiss Parliament decided to adjourn dealing with the motion until after the decision of the WTO dispute settlement bodies. It is now debatable whether a panel would find a ban in Switzerland “necessary”, taking into account the reasoning of the panel on the EU Seal regime.

<sup>40</sup> Appellate Body report, *China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products*, adopted 21 December 2009, WT/DS363/AB/R and Appellate Body report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, adopted 7 April 2005, WT/DS285/AB/R. See NICOLAS F. DIEBOLD, *The Morals and Order Exceptions in WTO Law: Balancing the Toothless Tiger and the Undermining Mole*, *Journal of International Economic Law* 11(1), 2008, pp. 43–74 for an in-depth analysis of the exception.

<sup>41</sup> See ROBERT HOWSE & JOANNA LANGILLE, *Permitting Pluralism: The Seal Products Dispute and why the WTO Should Accept Trade Restrictions Justified by Noninstrumental Moral Values*, *Yale Journal of International Law* 37, 2012, p. 367 on the justification of non-instrumental moral values in this connection.

<sup>42</sup> Motion vom 16. Juni 2011 eingereicht von Oskar Freysinger zum Importverbot für Robbenprodukte, 11.3635 n, online at <<http://bit.ly/1dReeba>> (9 April 2014).

<sup>43</sup> Verordnung vom 7. Dezember 2012 über die Deklaration von Pelzen und Pelzprodukten, SR 944.022.

## IV. Anti-Dumping Measures in China: *China – X-Ray Equipment*

In international trade, dumping occurs when manufacturers export a product to another country at a price either below the price charged in its home market or below the cost of its production (Art. VI:1 GATT).<sup>44</sup> Dumping may cause or threaten to cause injury to the industry of an importing country. The importing country is then allowed, when certain requirements are met, to take action and levy an anti-dumping duty on the dumped products in order to offset or prevent dumping and protect its own industry from injury (Art. VI:2 GATT).<sup>45</sup> The requirements for such actions are spelled out in the WTO Anti-dumping Agreement (ADA),<sup>46</sup> which contains provisions relating to methodology for determining dumping, injury and causation as well as procedural issues, to make sure that anti-dumping investigations are conducted in a transparent, objective and equitable way, with all interested parties being given adequate opportunity to defend their interests.<sup>47</sup>

Anti-dumping is one of the most litigated areas in the WTO. While recently anti-dumping disputes between developed countries have declined, such disputes have dramatically increased between developed and developing countries, especially since the admission of China into the WTO in 2001.<sup>48</sup> This tendency reflects the relative increase in the importance of developing countries in the global economy. According to the 2013 WTO Report of the Committee on Anti-dumping Practices, 30 WTO Members initiated a total of 209 new anti-dumping investigations from 1 July 2012 to 30 June 2013. China was the most frequent target for investigations, accounting for more than 25 per cent of all new initiations. Equally noteworthy is China's use of anti-dumping measures against its biggest trading partners. Until now China has been a party to 12 WTO anti-dumping disputes, which were settled with a panel or an Appellate Body report (6 as complainant and 6 as defendant).<sup>49</sup> The two following

<sup>44</sup> See PETER VAN DEN BOSSCHE & WERNER ZDOUC, *The Law and Policy of the World Trade Organization*, 3rd ed., Cambridge 2014, pp. 682 ff.

<sup>45</sup> See COTTIER & OESCH, *supra* n. 36, pp. 1016 ff.

<sup>46</sup> Agreement Establishing the World Trade Organization of 15 April 1994, Annex 1A, Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-dumping Agreement), SR 0.632.20.

<sup>47</sup> *In detail* JUDITH CZAKO, JOHANN HUMAN & JORGE MIRANDA, *A Handbook on Anti-Dumping Investigations*, Cambridge 2003.

<sup>48</sup> See LINGLING HE & RAZEEN SAPPIDEEN, *Mapping Anti-dumping Disputes from 1995 to 2011: The Changing Pattern*, *Journal of World Investment & Trade*, 13(1) 2012.

<sup>49</sup> LING LING HE, *China's Participation in Anti-Dumping Disputes*, *Frontiers of Law in China*, 7(4) 2012, pp. 616–646.

cases *China – X-Ray Equipment* and *China – Broiler Products* were decided in 2013.

## A. Facts

*China – X-Ray Equipment* is a dispute brought to the WTO on 25 July 2011 by the EU.<sup>50</sup> The dispute concerned X-ray security inspection equipment (scanners). These scanners are widely used in various types of security checks and customs inspections to detect dangerous articles, smuggled goods and suspicious substances concealed in bags, goods, containers or vehicles. In August 2009 the Chinese producer Nuctech Company Limited applied for the initiation of an anti-dumping investigation on European X-ray equipment exports to China. Of the two EU producers, only Smiths Heimann GmbH participated in the investigation of the Chinese Ministry of Commerce (MOFCOM). In its final determination MOFCOM imposed a 33.5 per cent anti-dumping duty on the import of X-ray equipment produced by Smiths and 71.8 per cent on imports from other EU sources, both for a period of five years. The EU exported X-ray equipment to China with an estimated worth of 70 million euro annually. The anti-dumping duties imposed essentially closed the Chinese market to imports of European X-ray equipment.

The EU challenged the anti-dumping duties imposed by China and the underlying investigation by MOFCOM before the WTO. The EU claims that the Chinese methodology for analysing the effects of EU exports on prices of X-ray equipment in China's domestic market is inconsistent with the requirement of Art. 3.1 and 3.2 ADA to conduct an objective examination of positive evidence to determine the injury to the industry (panel report, para. 7.30). The Chinese methodology involved comparing the weighted average unit values for the entire range of products covered by the investigation, without taking into account considerable differences among the products, especially between high-energy scanners for heavy cargo and low-energy scanners mainly used for luggage inspections. While EU exports were exclusively of cheaper low-energy scanners, China compared the prices of those with average unit values for the entire range of domestic products that included the very expensive high-energy scanners. The EU claims that making price comparisons without ensuring comparability does not amount to an objective examination of positive evidence and leads to a distorted price effect analysis (para. 7.34). China argued that MOFCOM compared the prices of "like" products, which was sufficient to ensure price comparability and did not distort its price effect analysis (para. 7.65).

<sup>50</sup> Third parties: Chile, India, Japan, Norway, Thailand and United States.

The EU also alleged that MOFCOM failed to respect certain due process and transparency requirements provided for by the ADA. In particular, the EU claims that China acted inconsistently with Art. 6.5.1 ADA because MOFCOM failed to ensure a proper summary of confidential information that Nucotech submitted regarding two models to calculate the dumping margin in their application (para. 7.305), the EU claimed further that China acted inconsistently with Art. 6.9 ADA because MOFCOM failed to disclose essential facts during the investigation, such as the methodology and the underlying data used in its price effect analysis (para. 7.378), and finally the EU claimed that China acted inconsistently with Art. 12.2.2 ADA because MOFCOM failed to include in its public notice certain essential facts, which justified the imposition of final measures, and the arguments of the cooperating EU producer (para. 7.430). China defended MOFCOM's investigation arguing that the summaries were adequate and could not be more detailed without compromising confidentiality (para. 7.334), that the methodology used to consider price effects of the dumped imports does not constitute facts, and if it would be considered facts, not essential facts that need to be disclosed (para. 7.389) or included in the public notice (para. 7.445) and that its explanation as to why it rejected certain arguments of the cooperating EU producer in the public notice was adequate and sufficient (para. 7.541).

## B. Findings

On the most important substantive issue in *China – X-Ray Equipment* the panel considered whether it is necessary to take into account differences in the products being compared when conducting a price effect analysis. The panel agreed with the Appellate Body in the recent *China – GOES* case that “when a price comparison is made for the purposes of an undercutting analysis [...] it is necessary to ensure that the prices being considered are actually comparable”.<sup>51</sup> The necessity of comparability arises out of “a logical progression of inquiry [in Art. 3 ADA] leading [from the price comparison] to an investigating authority’s ultimate injury and causation determination”.<sup>52</sup> The panel did not agree with MOFCOM’s conclusion that within the broad product scope of the investigation (scanners used to detect objects), all the domestic products were “like” the imported products (para. 7.65). The panel underlined that where a broad basket of imported goods and a broad basket of domestic goods have been

<sup>51</sup> Appellate Body report, *China – Countervailing and Anti-Dumping Duties on Grain Oriented Flat-rolled Electrical Steel from the United States*, adopted 16 November 2012, WT/DS414/AB/R, para. 200.

<sup>52</sup> *Ibid.* para. 128.

found to be “like” by the investigating authority, this does not automatically mean that each of the goods included in the basket of domestic goods is “like” each of the goods included within the scope of the imported products (para. 7.65).<sup>53</sup> The panel held that there was enough evidence to put MOFCOM on notice that dumped imports consisted only of low-energy scanners, while there was no such limit on the energy level of the domestic like product and that price comparability therefore was an issue (para. 7.68). On this basis, the panel concluded that China acted inconsistently with Art. 3.1 and 3.2 ADA because China had failed to ensure that the prices it was comparing were actually comparable and therefore the price effect analysis was not based on an objective examination of positive evidence (para. 7.97).

On procedural issues the panel agreed with the EU that MOFCOM failed to respect certain due process and transparency requirements provided for by the ADA. In particular, the panel decided that China failed to ensure a proper summary of certain confidential information and therefore acted inconsistently with Art. 6.5.1 ADA citing the panel in *Mexico – Olive Oil* “that confidential information should usually be capable of being summarized [without compromising confidentiality]” (Para. 7.334).<sup>54</sup> The panel further decided that MOFCOM failed to disclose the annual average unit value it used in its price effect analysis and the underlying price data as essential facts that formed the basis for their decision to apply definitive measures and therefore China acted inconsistently with Art. 6.9 ADA (para. 7.402). And finally the panel decided that China had failed to provide in public notice how the findings of the price effect analysis were reached and had also failed to explain why it rejected arguments made by the respondent and, therefore, China had acted inconsistently with Art. 12.2.2 ADA (para. 7.461).

## **V. Anti-Dumping Measures in China: *China – Broiler Products***

### **A. Facts**

*China – Broiler Products* is a dispute brought to the WTO on 20 September 2011 by the US.<sup>55</sup> Broilers are chickens bred and raised specifically for meat

<sup>53</sup> See also Panel report, *European Communities – Anti-Dumping Measure on Farmed Salmon from Norway*, adopted 15 January 2008, WT/DS337/R, paras. 7.13–76.

<sup>54</sup> Panel report, *Mexico – Definitive Countervailing Measures on Olive Oil from the European Communities*, adopted 21 October 2008, WT/DS341/R, para. 7.90.

<sup>55</sup> Third parties: Chile, European Union, Japan, Mexico, Norway, Thailand and Saudi Arabia.

production. Broiler products include nearly all chicken products, aside from live, cooked, and canned chicken. Specifically, the dispute centred on chicken paws (an industry term for chicken feet). In China such chicken paws are a popular snack, often washed down with a beer, while in the US they are considered practically worthless by-products useful only for being ground into pet food. Once this unexpected trade synergy was discovered more than a decade ago, US exports of chicken paws grew rapidly from virtually nothing to 377,805 metric tons, worth US\$ 278 million in 2009.<sup>56</sup> In the same year the China Animal Agriculture Association lodged a complaint with MOFCOM about the selling of US-exported chicken-paws at below-market cost. In its final determination MOFCOM levied an anti-dumping duty ranging from 50.3 to 53.4 per cent for the three big US broiler product export companies which cooperated in China's investigation (Tyson Foods, Pilgrim's Pride and Keystone Foods; the respondents) and at 105.4 per cent for the others, all for a five-year period.<sup>57</sup> Since the imposition of the trade remedies, US broiler trade with China has collapsed by 90 per cent and the industry has lost exports with an estimated worth of USD 1 billion.<sup>58</sup>

Like in the previous case, in *China – Broiler Products* the US challenged the anti-dumping duties imposed by China and the underlying investigation by MOFCOM before the WTO. The key issue in *China – Broiler Products* revolved around the question of how to allocate production costs, and later determine dumping margins, where the products at issue are split-off or by-products like the chicken paws.<sup>59</sup> The US broiler export companies used the value-based allocation method. Pre-split-off costs are allocated to the various final products (breast meat, wings, chicken paws etc.) according to the proportion of revenue generated by the sale of those products. This method is in accordance with generally accepted accounting principles (GAAP) in both the US and China. MOFCOM, however, rejected this method and used the weight of the particular chicken product to allocate pre-split-off costs. The US claims that China acted inconsistently with Art. 2.2.1.1 ADA because MOFCOM declined to use the respondents' normal books and records, most importantly their cost allocations, without explaining the reason for their decision not to do so and that MOFCOM's weight-based cost allocation did not reasonably reflect the cost of

<sup>56</sup> KEITH B. RICHBURG, U.S., China embroiled in trade spat over chicken feet, *The Washington Post*, 16 December 2011, online at <<http://wapo.st/1fSqnAZ>> (9 April 2014).

<sup>57</sup> China also imposed countervailing duties based on subsidization. This contribution however will only deal with the anti-dumping claims and not with the claims under the Agreement on Subsidies and Countervailing Measures.

<sup>58</sup> RICHBURG, *supra* n. 56.

<sup>59</sup> Products that begin the production process as a single product, but are subsequently broken up into separate products, which are sold or exported.



production (para. 7.108). China, in contrast, held that the respondents' normal books and records did not reasonably reflect the cost associated with the production and sale of the product under consideration. Despite having significant global sales, China argued that the respondents only used revenue from US sales in determining the cost allocation. Even though chicken paws have value in both the domestic and export markets, the respondents treated them as by-products, allocating none of the pre-split-off costs to these products (paras. 7.109 and 7.168). This finding is highly relevant for the US, because with the value-based cost allocation method, a very low level of production costs is added to the chicken paws. Accordingly, the high prices in China for these products would exceed the low production cost of the products and consequently there would be no dumping margin.

The US made further similar claims to the ones of the EU discussed above in *China – X-Ray Equipment*. The US made a substantive claim that China failed to ensure price comparability because MOFCOM compared all domestic broiler products to the imported products from the US, which primarily consisted of chicken paws. The US also made procedural claims, including that China had failed to provide adequate non-confidential summaries, to disclose all of the essential facts underlying its price effect analysis and to provide the reasons for its rejection of the US's and interested parties' arguments. China again contested all of these claims.

## **B. Findings**

On the key issue in *China – Broiler Products* the panel held that an investigating authority should normally use the books and records of the respondent to calculate the costs of production, but it retains the right to decline to use such data, if it is clearly shown that the books and records are either inconsistent with GAAP or do not reasonably reflect the costs of production (para. 7.164). The burden of proof is not on the respondent to demonstrate in the first place why their books and records reasonably reflect the costs of production, especially where their historically-used method is GAAP-consistent, as in this case. The panel further held that while MOFCOM made a summary statement that respondents' costs did not reasonably reflect the production cost for the chicken paws, it failed to provide the supporting reasoning (para. 7.171). The panel acknowledged that the arguments raised by China (determination of chicken paws' value based only on revenue from US sales and the treatment of chicken paws as by-products without allocating any pre-split-off costs to them) could serve as a basis for determining that the books and records do not reasonably reflect the costs of production for the chicken paws. The panel was however unable to conclude, based on the record of MOFCOM's investigation, that the

concerns expressed by China before it were indeed the reasons why MOFCOM departed from the rule of using a respondent's books and records. The panel also found no evidence in the record of the investigation to support MOFCOM choice to apply the weight-based methodology over the alternatives proposed by the respondents. In addition, the panel pointed out that MOFCOM's straight allocation of total processing costs to all products necessarily means that it included costs solely associated with processing certain joint products in its calculation of costs to all subject broiler products (para. 7.196). The panel found that this does not reasonably reflect production costs. Thus, the panel concluded that China acted inconsistently with Art. 2.2.1.1 because MOFCOM failed to explain both its refusal to use the value-based cost allocation method in the books and records of the respondents and the use of its own weight-based cost allocation method, which after all did not reasonably reflect the cost of production (para. 7.198).

Regarding the US claims, similar to the claims of the EU in *China – X-Ray Equipment* the panel found that China failed to comply with the same substantive and procedural requirements that China had already been faulted for in *China – X-Ray Equipment*.

### **C. Commentary**

The two anti-dumping cases are of importance for four reasons. Firstly, from the perspective of trade regulation *China – Broiler Products* was the first case to address the complex issue of how to determine dumping margins for joint, split and by-products. The panel held that both the value- and weight-based cost allocation methodologies might be reasonable. Countries conducting anti-dumping investigations should be careful to clearly justify and explain their reasons when they deviate from the cost allocation method the companies use in their books and records. Furthermore, both cases showed that complainants should not focus on whether investigating authorities define the products under consideration too broadly (e.g. include all scanners) to properly match the domestic like product, but instead argue that the price effect analysis is affected by the existence of a range of products, especially where only the cheapest products in the range are exported.

Secondly, the findings of the panels will in the end strengthen the rule of law in Chinese anti-dumping investigations. China failed in both cases to successfully defend MOFCOM's due process and transparency shortcomings on fundamental issues such as the disclosure of essential facts underlying a decision, providing fora for adverse parties to defend their interests, making available evidence in public notice etc. The law and the dispute settlement system of the WTO develop considerable influence in rendering parts of the Chinese admin-

istrative practice more predictable and more accountable. China is still in its early stages of anti-dumping litigation at the WTO and mastery of the procedural requirements of the ADA is key to defending its anti-dumping duties, which will be more and more important as China's global market share increases.

Thirdly, from a world trade perspective, the anti-dumping duties challenged in both cases are sometimes associated with tit-for-tat retaliation by China for previous lost trade disputes and leave a slight impression of bad faith use of trade remedies. The Chinese anti-dumping duties challenged by the EU in *China – X-Ray Equipment* may be seen as a reaction to the introduction of definitive anti-dumping duties on cargo scanners by the EU in 2010.<sup>60</sup> The duties challenged by the US in *China – Broiler Products* may be a response to duties on Chinese tyre exports to the US put in place in 2009, which China unsuccessfully challenged in the WTO,<sup>61</sup> or generally placed in the context of increasing trade frictions between the US and China.<sup>62</sup> In neither case did China appeal the findings of the panel, which may indicate that the trade remedies were motivated by retaliation rather than genuine concerns about injurious dumping. The two reports send a strong signal that, while WTO Members have the right to use trade remedies, this right cannot be abused and must be exercised in line with WTO rules.

Fourthly, from a Swiss perspective it is very important to take into account the Chinese experiences with anti-dumping dispute settlement in the WTO. Switzerland is only the second country in Europe to sign a free trade agreement (FTA) with China.<sup>63</sup> In Art. 5.2 of the FTA the parties agreed that their rights and obligations in respect of anti-dumping measures should be governed by Art. VI GATT and the WTO ADA. Furthermore, the parties agree not to take such measures in an arbitrary or protectionist manner and prior bilateral consultations between the parties are foreseen. Rights and obligations in the FTA between China and Switzerland, it would seem, do not transgress WTO law. Time will tell whether these provisions will come to bear to the extent that China will export its own allegedly dumped products from Switzerland into other countries, in particular the EU. In such cases, the EU will not accept

<sup>60</sup> The EU Trade Commissioner KAREL DE GUCHT said in response to the panel ruling: "I will not accept tit-for-tat retaliation against European companies through the misuse of trade defence instruments." online at <<http://bit.ly/1In99Py>> (9 April 2014).

<sup>61</sup> See Appellate Body report, *United States – Measures Affecting Imports of Certain Passenger Vehicle and Light Truck Tyres from China*, adopted 5 October 2011, WT/DS399/AB/R.

<sup>62</sup> RICHBURG, *supra* n. 56.

<sup>63</sup> Free Trade Agreement between the Swiss Confederation and the People's Republic of China from 6 July 2013, signed and approved by Parliament, but not yet ratified as of 9 April 2014.

Swiss origin of the products, but rely upon its autonomous rules of origin in accordance with Art. 24 and 25 of the Community Customs Code.<sup>64</sup>

<sup>64</sup> See EDWIN VERMULST & DAVIDE ROVETTA, Origin Rules in EU Anti-dumping Law and Practice: an Update, *Global Trade and Customs Journal* 3(10) 2008, p. 337; Regulation (EC) No 450/2008 of the European Parliament and the Council of 23 April 2008 laying down the Community Customs Code (Modernised Customs Code), 2008 OJ L 145/1.

