I. INTRODUCTION

1.1 On 12 June 1998, the European Communities requested consultations with the United States pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), Article XXII:1 of the General Agreement on Tariffs and Trade 1994 (GATT 1994) and Article 30 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement) with respect to the imposition of countervailing duties by the United States on certain hot-rolled lead and bismuth carbon steel products (leaded bars) originating in the United Kingdom in the context of three successive annual reviews (WTO document WT/DS138/1). The European Communities and the United States held consultations on 29 July 1998, but failed to reach a mutually satisfactory solution.

1.2 On 14 January 1999, pursuant to Articles 4 and 6 of the DSU, Article XXIII of the GATT 1994 and Article 30 of the SCM Agreement, the European Communities requested the establishment of a panel with respect to the imposition of countervailing duties by the United States on certain hot-rolled lead and bismuth carbon steel products originating in the United Kingdom in the context of three successive annual reviews (WTO documents WT/DS138/3 and WT/DS138/3/Corr.1).

1.3 At its meeting on 17 February 1999, the Dispute Settlement Body (DSB) established a panel pursuant to the above request. At that meeting, the parties to the dispute agreed that the Panel should have standard terms of reference. The terms of reference were:

> "To examine, in light of the relevant provisions of the covered agreements cited by the European Communities in documents WT/DS138/3 and WT/DS138/3/Corr.1, the matter referred to the DSB by the European Communities in that document and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements".

1.4 On 16 March 1999, the Panel was constituted as follows:

Chairman: Mr. Ole Lundby

Members: Mr. Paul O'Connor

Mr. Arie Reich

1.5 Brazil and Mexico reserved their rights as third parties to the dispute.

1.6 The Panel met with the parties on 15-16 June 1999 and 14-15 July 1999. It met with the third parties on 16 June 1999.

1.7 The Panel submitted its interim report to the parties on 6 October 1999. On 20 October 1999, both parties submitted written requests for the Panel to review precise aspects of the interim report. On 8 November 1999, each party filed comments on the written request submitted by the other party. Neither party requested a further meeting with the Panel. The Panel submitted its final report to the parties on 22 November 1999.

II. FACTUAL ASPECTS

2.1 This dispute concerns the imposition of countervailing duties by the United States on certain hot rolled lead and bismuth carbon steel products originating in the United Kingdom in the context of three successive annual reviews.

2.2 On 8 May 1992, a countervailing duty investigation was initiated by the United States against imports of hot rolled lead and bismuth carbon steel from, *inter-alia*, the United Kingdom. The period of investigation was calendar year 1991. On 27 January 1993, the United States Department of Commerce (USDOC) issued a final determination establishing a subsidy rate of 12.69 per cent on imports from United Engineering Steels Limited (UES).[1] On 22 March 1993, following an affirmative injury determination by the United States International Trade Commission (USITC), the USDOC published a countervailing duty order at the above rate on imports from UES.

2.3 During the period of investigation, UES was a joint-venture equally owned by British Steel Public Limited Company (British Steel plc) and Guest, Keen and Nettlefolds (GKN), both of which were privately-owned companies.

[1] Final Affirmative Countervailing Duty Determination: *Certain Hot Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*. Federal Register, 27 January 1993, Vol. 58, No. 16, pp. 6237-6246.

The alleged subsidies countervailed were not provided to either co-owner of UES but to state-owned British Steel Corporation (BSC). BSC established UES in 1986 in association with GKN. British Steel plc was related to BSC in the sense that the former assumed the property, rights and liabilities of the latter in September 1988. The British government privatized British Steel plc in December 1988 through a sale of shares. Both parties agree that the privatization of British Steel plc was "at arm's length, for fair market value and consistent with commercial considerations".

2.4 On 21 March 1995, UES became a wholly-owned affiliate of British Steel plc as this company bought out GNK's interests. UES was subsequently renamed British Steel Engineering Steels (BSES).

2.5 The alleged subsidies countervailed relate principally to equity infusions granted by the British Government to BSC during fiscal years 1977/78 - 1985/86. The USDOC classified such alleged subsidies as non-recurrent and thus spread them out over 18 years, deemed to be the useful life of productive assets in the steel industry. The USDOC found that the alleged subsidies in question "passed through" from BSC to UES first, and then more recently to BSES.

2.6 Following the original imposition of CVDs in March 1993, the DOC has undertaken six annual reviews to set the duty rate on imports of the subject product. The first review is not being challenged as it was initiated on 15 April 1994, prior to the entry into force of the SCM Agreement. The fifth review, initiated on 24 April 1998, is not being challenged either as it was completed (11 August 1999) after the request for establishment of the Panel (WTO documents WT/DS138/3 and WT/DS138/3/Corr.1). Similarly, the sixth review, initiated on 30 April 1999, is not subject to challenge given that it was opened after the request for establishment of the Panel. Therefore, the subject of this Panel are the outcomes of the second, third and fourth reviews, initiated in 1995, 1996 and 1997, respectively. UES and BSES were the only exporters involved in these reviews.[2]

2.7 The 1995 review, covering imports during calendar year 1994, was initiated on 14 April 1995 and was completed on 14 November 1996.[3] In this review, the USDOC determined a subsidy rate of 1.69 per cent on imports from UES.

2.8 The 1996 review, covering imports during calendar year 1995, was initiated on 25 April 1996 and completed on 14 October 1997.[4] In this review, the USDOC established two separate subsidy rates on account of the fact that UES transformed itself into BSES during the period of review. In particular, the USDOC established a subsidy rate of 2.40 per cent, applicable to imports from UES made during the period 1 January 1995 through 20 March 1995, and an-

2 Allied Steel and Wire Limited (ASW Limited) was involved in the original 1992 investigation as well as in the 1994 review. However, this company has not participated in any subsequent reviews.

3 *Certain Hot-Rolled Lead and Bismuth Carbon Steel Products from the United Kingdom*; Final Results of Countervailing Duty Administrative Review. Federal Register, 14 November 1996, Vol. 61, No. 221, pp. 58377-58383.

4 Ibid., 14 October 1997, Vol. 62, No. 198, p. 53306.

other subsidy rate of 7.35 per cent, corresponding to imports from BSES during the period 21 March 1995 through 31 December 1995.

2.9 The 1997 review, covering imports during calendar year 1996, was initiated on 29 April 1997 and was completed on 15 April 1998.[5] In this review, the USDOC determined a subsidy rate of 5.28 per cent on imports from BSES.

III. ARGUMENTS OF THE PARTIES

3.1 The arguments of the parties are set out in their submissions to the Panel (see Attachments 1.1 through 1.7 for the European Communities and Attachments 2.1 through 2.8 for the United States).

IV. ARGUMENTS OF THE THIRD PARTIES

A. *Brazil*

Brazil made the following written arguments as third party:

4.1 In the past decade, the US Government has issued a series of countervailing duty decisions regarding privatization. These decisions have affected, and continue to affect, a wide variety of products and countries, including Brazil. In the view of the Government of Brazil, the US Government's analysis of privatization has led consistently to countervailing measures (hereinafter CVDs) contrary to the US international obligations under the GATT 1994, and the Agreement on Subsidies and Countervailing Measures ("SCM Agreement").

4.2 The US actions and findings are inconsistent with its obligations under the SCM Agreement in two significant respects. First, the US analysis fails to recognize a duty intrinsic to Article 1 of the SCM Agreement to analyse and detect the conferral of benefits to a company during the period of investigation. This duty includes an obligation to consider all information relating to developments, such as changes in ownership, subsequent to an initial financial contribution.

4.3 The US argues that the SCM Agreement creates no duty to consider the impact of subsequent events on the flow of benefits after an initial subsidy event is detected. The US argues it can presume, irrebutably, that the benefits of an initial subsidy event continue to flow to the new owners of an asset or company even after an arm's-length sale or privatization. This irrebuttable presumption, in and of itself, is inconsistent with the Article 1 of the SCM Agreement.

4.4 Second, given this obligation to find a benefit conferred to the company subject to investigation during the period of investigation, it is relevant how an arm's length sale affects and eliminates the conferral of benefits from a pre-sale subsidy to the purchaser. An analysis of benefit, consistent with the SCM Agreement, leads to the conclusion that a purchaser of assets (or a company) in an arm's length transaction does not receive any benefit from pre-sale infusions.

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5 Ibid., 15 April 1998, Vol. 63, No. 72, pp. 18367-18375.

4.5 Brazil believes it important for the panel to recognize that the US Government practice impacts its CVD decisions with respect to privatizations and changes in ownership in a variety of countries, including Brazil. With respect to all forms of arm's length privatizations, the basic flaws in analysis lead to the same basic violations of SCM Agreement principles.

4.6 Brazil provides a general framework for analysing pre-privatization subsidies. This framework will assist the panel in reaching a determination that addresses the flaws in the US decisions at a basic level. In this manner, the US will be forced to revise the fundamental premises of its analysis, and bring its practice for all privatization decisions into conformance with the SCM Agreement.

4.7 In addition, Brazil supplements the discussion in the First Submission of the European Communities ("EC") with additional legal analysis that applies to the underlying dispute between the US and EC, as well as other circumstances. In particular, Brazil addresses the general requirement under the SCM Agreement to identify and measure benefits of a subsidy on a basis that is specific to the company under investigation, during the period of investigation. Brazil identifies support for this requirement that supplements that addressed in the EC submission.

4.8 With respect to the impact of an arm's-length privatization, Brazil adds to the discussion in the EC submission by observing that it is always critical to focus on the "ownership relationship" between an owner and an asset (or the assets of a company in a privatization) and the terms of acquisition in determining whether a benefit exists. An examination of the owner/asset relationship is the only logical form of analysis that can support a determination that a benefit does or does not exist.[6] By framing its analysis in these terms, the panel's decision will address the underlying issues in this proceeding, and lay a foundation for any future consultations and disputes between the US and other WTO Members related to privatization.

2. *Framework for analysis of pre-privatization subsidy benefits*

4.9 The question before this panel is most simply stated as whether the benefits of financial contributions made by a government or government entity to a company continue after the company that received the financial contribution has been privatized. Specifically, the question is whether the benefits of government equity infusions in government-owned companies survive the privatization of the government owned company when that privatization transfers ownership or assets to non-government entities at a fair market value.

4.10 While Article 14 of the Agreement is intended to focus on the calculation of the amount of the subsidy based on the benefit to the recipient, it is instructive in providing guidance as to what is and what is not a benefit. In terms of govern-

6 After a change in ownership, the US applies countervailing duties primarily to pre-privatization grants and equity infusions. Thus, for the purposes of this submission, Brazil focuses on the benefits of these two forms of subsidies.

ment provision of equity capital, paragraph (a) provides that a benefit is conferred only when such provision of equity capital is on terms "inconsistent with the usual investment practice of private investors." This benchmark of consistency with market driven policies is confirmed by paragraphs (b), (c) and (d) which all reference "commercial" or "market" criteria as the basis of determining whether a benefit has been and continues to be conferred.

4.11 With respect to some categories of benefits, the event that extinguishes the benefit is obvious. For example, if the benefit is in the receipt of below market interest on a loan from the government or a government entity, there is a benefit only so long as the loan is outstanding and the interest charged on that loan is lower than the interest that would be charged on a comparable commercial loan. Thus, the benefit ends if either the interest on the loan principal is altered to reflect commercial interest rates or if the loan itself is no longer outstanding.

4.12 The value of the benefit will, in turn, vary depending on the amount of the principal which is outstanding and the relationship between the below market interest rate and the commercial interest rate. Thus, the existence of benefits and the value of the benefits conferred can change with events which occur after the initial action by the government or government entity conferring a benefit.

4.13 A simple example, using a pencil, illustrates how benefits and the party receiving the benefits can change over time. If a Government gives Company A a pencil, the benefit to Company A is the value of the pencil. If Company A sells the pencil at fair market value to Company B, the benefit of the Government's action still resides with Company A not Company B, since A has retained the value of the pencil in the form of cash and B has paid Company A the same amount for the pencil as it would have paid on the open market. The asset has been transferred, but the benefit remains in Company A.

4.14 Let's assume that rather than selling the pencil immediately, Company A uses half of the pencil and then sells the remaining portion of the pencil to Company B. Company B again pays fair market value, but it pays only fair market value for half a pencil since that it all it is receiving. Company B has received no benefit because it has paid market value for the pencil. Company A has a residual benefit - the value received from Company B for half the pencil. The remainder of the benefit has been used in the form of the half of the pencil which Company A has already consumed.

4.15 Finally, assume that Company A never sells the pencil but uses it until it is finished. Under this scenario, Company A has received all of the benefits. However, after finishing the use of the pencil, no additional benefits exist. To assume benefits continue after the pencil is fully used would be to attribute benefits to Company A in terms of receiving the pencil in excess of the value of the pencil.

4.16 The analysis with respect to government provision of equity capital is really no different than the analysis of benefits where the government provides funding, goods or services at no cost or below cost to an entity. Rather than getting nothing in exchange for the funding, goods or services provided, the Government gets a share of the company and, therefore, of its assets and liabilities. In essence, it simply owns a share of the benefits received by Company A as a result of the funding, goods or services provided by the government on terms inconsistent with commercial considerations.

4.17 Let's assume, for example, that in the above example Company A is owned by the government and receives an equity investment equivalent in value to a pencil. Company A uses the equity investment to buy a pencil. Company A then sells the pencil to Company B at its market value. The benefit remains in Company A. It has simply converted a cash infusion in terms of equity into an asset and then reconverted the asset into cash by selling that asset. Company B has not received any benefit because it paid market value for the asset it acquired from Company A.

4.18 Let's further suppose that the government has decided that it no longer wants to own Company A - i.e. it is going to privatize the company. Company A's only asset is the pencil and it has no liabilities. In the privatization, the equity shares of Company A are valued at the net of its assets and liabilities, in this case the value of the pencil. Rather than purchase the pencil itself, Company B purchases all of the equity in Company A and pays the market value of its net worth (again, the value of a pencil) to acquire the equity. Company B has received no benefit in that it has paid the fair market value for its equity purchases based on the underlying value of the company whose shares have been bought. The benefit previously conferred on Company A has been transferred to the prior shareholders in Company A through the purchase at market value of the shares in Company A. Because Company A was owned by the government, in effect the benefit has been returned to the government.

4.19 While the case being examined by the panel is more complex factually than the pencil example, the pencil example illustrates the crucial point in any analysis of benefits under the Agreement: whether you purchase an asset (the pencil) or the ownership interest in an asset (i.e. equity), neither the asset (the pencil) nor the ownership interest in the asset (the equity in the company which owns the asset) continues to have a benefit conferred on it if the new owner has paid market value for the asset or the ownership interest in the asset. The benefit remains with the original owner of the asset or the ownership interest in the asset if the new owner pays market value to the original owner.

2. *Brazil's privatization programme was structured to eliminate pre-privatization subsidy benefits*

4.20 The privatization issue is of particular importance to Brazil, since it has undertaken a vast privatization programme, including the privatization of all formerly state-owned steel mills. The pre-privatization equity infusions to the steel mills were investigated beginning in 1983. The benefits of these equity infusions after privatization were first investigated by the US authorities in 1992/1993 and determined to remain in the privatized company. This investigation involved the first of the privatized mills, USIMINAS. The US has preliminarily reached the same conclusion in a current investigation of USIMINAS and two other privatized mills.

4.21 Ironically, the Brazilian privatization programme was structured with the specific intention of eliminating any benefits from the Government to the privatized steel mills. That is, the process devised by the Government ensured that the mills were sold at a market determined value. This result was achieved through a careful valuation process involving studies by two independent groups, the setting of minimum prices for each mill based on these studies, and the use of an auction process to ensure that market forces ultimately determined the price for each mill.

4.22 The current owners do not enjoy any benefits, having paid a market determined price for the mills. To the extent that any residual benefits of government equity infusions existed at the time of the privatization, these benefits were included in the valuation of each mill and, therefore, in the price paid. As such, no advantage was conferred on the new owners.

4.23 If pre-privatization provisions of equity capital were deemed to confer a benefit because the investment decision was inconsistent with usual investment practices as required by Article 14(a) of the SCM Agreement, then the sale of equity based on investment decisions which are consistent with usual investment practices by definition cannot confer a subsidy. In ensuring that the new owners of the mills paid a market determined price for the mills, Brazil ensured that no benefits of equity infusions in the pre-privatized companies continue to benefit the privatized companies.

3. A plain interpretation of the provisions of the SCM Agreement requires an affirmative finding of the conferral of a benefit to a company during the relevant period

4.24 As its initial defence, the US argues that it is not required under the SCM Agreement to recognize the absence of benefits to the purchaser of an asset or company in an arm's length transaction. At the heart of the US position is the premise that under SCM Agreement Articles 1 and 14, there is no requirement to analyse the existence and value of a benefit after the initial financial contribution. The US interpretation of Articles 1 and 14 is without support. A plain interpretation of these Articles demonstrates that the SCM Agreement requires a finding and measurement of a benefit to a company during a particular period.

4.25 Article 1 of the SCM Agreement establishes the very foundations of any determination to apply countervailing measures. As a precondition to a countervailable subsidy determination, Article 1 requires three affirmative findings:

- a financial contribution by a government (Article 1.1(a)),
- that the financial contribution thereby confers a benefit (Article 1.1(b)); and
- that the first two elements above were provided on a specific basis (Article 1.2).

4.26 The second finding involves an obligation on the part of the investigating authority to determine whether the company subject to investigation received a countervailable benefit during the period of investigation. It is not sufficient, as discussed in the EC submission, to find that a benefit is conferred to some other company, during some other period, and presume that the benefit is conceptually transferred to the company subject to investigation, and this transferred benefit is received during the period of investigation. With each company and investigation, the investigating authority is obligated to find a continuing nexus between the underlying financial contribution, and a benefit to that company during that period.

4.27 The US position relies on the view that there is no obligation to find that the firm under investigation was the recipient of the subsidy. See e.g., paragraph 156 of the US First Submission. The primary argument is that the "ordinary meaning" of Article 1 does not require a finding of benefit specific to the company subject to investigation, during the period of investigation. Rather, the US argues that Article 1 permits Members to detect and measure subsidy benefits only as of the moment of subsidization, and then allocate benefits based on that initial finding, regardless of subsequent developments.

4.28 Thus, the US position is premised on a limited interpretation of the phase "a benefit is thereby conferred" to refer to the company that initially receives the subsidy, and the period in time when the financial contribution is initially made. The US argues that Article 1.1(b) obligates Members to find and measure the conferral of a benefit only as of the moment of the financial contribution.

4.29 The US position is in direct conflict with interpretations by the EC, Brazil and other members, that contemplates the detection of the conferral of the benefit (i.e., the continuation of the benefit) to the company subject to a particular investigation, during the relevant period of investigation. This difference in the interpretation of the intended timing of the duty under Article 1.1(b) separates the US from the EC, Brazil, and other WTO Members.

4.30 The panel should resolve this dispute as to the meaning of Article 1.1(b) by considering several relevant factors.

4. *Under the SCM Agreement, CVD investigations focus on benefits to companies during particular periods of time, regardless of the timing of the conferral of underlying subsidies*

4.31 The US is proposing an interpretation of "is thereby conferred" that is inconsistent with the mechanics and operation of the SCM Agreement, as well as other similar agreements, such as the Agreement on Implementation of Article VI of the GATT 1994 ("AD Agreement"). The US interpretation ignores the fact that CVD investigations in the US (and in most other Member countries), are company specific, and period specific.[7] The initial task in a CVD investigation is to focus on whether a particular company, during a particular period, benefited from subsidies. If so, the next step is to formulate a methodology that measures precisely what the benefit was during a particular period.

[7] Although more than one company may be involved in a CVD investigation, the US calculates a company-specific CVD rate for each company subject to investigation.

4.32 The ultimate objective in calculating the benefit conferred during the particular period is to identify a countervailing duty that is properly correlated to the underlying benefit. The fundamental duty at the core of Part V of the SCM Agreement - to calculate a countervailing duty that offsets no more than the benefit to a company's exports. All actions pursuant to Article 1 and 14 must be directed towards this objective. The approach proposed by the US invites an unjustified separation between the actual benefit conferred to a company during a particular period, and the calculation of a countervailing duty to be applied to the exports of that company.

4.33 Interestingly, in its implementation of the SCM Agreement, US law agrees with the interpretation of the EC, Brazil and other WTO Members. Section 703(b)(1) specifically requires a determination that "a countervailable subsidy is being provided with respect to subject merchandise" (emphasis added). Thus, US law recognizes that there must be a present benefit to the specific merchandise under investigation.

4.34 Given this immediate focus on a specific period, on a specific company, the phrase "a benefit is thereby conferred" can only refer to the company subject to investigation, during the period of investigation. It does not matter if the period investigated is contemporaneous with, or significantly after, the time the actual subsidy was bestowed. The broader, more obtuse, interpretation of "is thereby conferred" advanced by the US is simply not credible.

5. *The SCM Agreement has a bias against irrebuttable presumptions of fact over periods of time*

4.35 The US interpretation is inconsistent with other aspects of the SCM Agreement and other similar WTO agreements. The SCM Agreement, like the AD Agreement, circumscribes limited areas in which Members may make determinations, and then presume that this determination is valid for a period of time. With respect to most determinations, the SCM Agreement, like the AD Agreement, contemplates a consideration and incorporation of all relevant and current information in making a finding.

4.36 Thus, there is a pervasive bias in the SCM Agreement against presumptions that endure unchallenged over time. However, the US interpretation inserts such an unchallengable presumption in the finding of a benefit. In the underlying proceeding, the US argues that its finding and measurement of a benefit should not be revisited for 18 years, the amortization period for the benefits received by British Steel Corporation before its privatization.

4.37 The most telling example of a bias against the extended validity of a factual presumption is the requirement for regular reviews. The SCM Agreement, like the AA contemplates regular reviews of CVD findings. Such reviews are provided for in Article 21 of the SCM Agreement. In each of these reviews, the validity of the prior CVD findings is revisited. From review to review, the flow of a benefit may change, a subsidy may be withdrawn, and the value of the company's sales may change (thereby altering the ad valorum calculation), to name a few of the factors examined in a review.