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WTO Dispute Settlement and Industrial Policy

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New Industrial Policy and the Trade System

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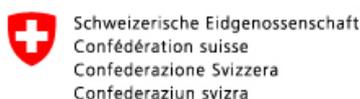
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ABSTRACT

Taking a detailed look at the World Trade Organization (WTO) dispute settlement mechanism in relation to the space it provides for Member countries' industrial policies, this paper examines whether and how existing decisions of WTO panels and the Appellate Body have affected, or expanded, the policy space for Members to pursue industrial policies under WTO law. It also looks into how such policy space could be further expanded through WTO panel and Appellate Body decisions.

First, the paper presents general conceptual reflections on how WTO dispute settlement can influence the policy space available to WTO Members to adopt industrial policy measures. These conceptual reflections address the role of WTO panels and the Appellate Body in general; the nature and categorization of WTO legal provisions applicable to trade in goods; and the interpretation of categories of rules most likely to impact the policy space of WTO Members. Second, the paper discusses two cases in which the Appellate Body interpreted certain WTO provisions in a manner that arguably creates more policy space for industrial policy measures than alternative interpretative approaches would have permitted. Third, it considers other potential examples of how WTO dispute settlement decisions could create or enlarge policy space under other WTO legal provisions with respect to industrial policy measures.

The paper points to a number of examples of how existing or potential interpretations and findings of WTO adjudicatory bodies may impact on the policy space of WTO Members to implement industrial policy measures. The many examples demonstrate that WTO dispute settlement can, at the margin and in some instances, affect the policy space available for Members to pursue industrial policy objectives. The dispute settlement bodies may also, through their interpretation and application of the law, influence the willingness of potential claimants to bring challenges before the WTO. However, it bears repeating that the ability of dispute settlement decisions to impact WTO Members' policy space for industrial policy is strictly circumscribed by the existing treaty rules that WTO panels and the Appellate Body have to take as a given.

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LIST OF ABBREVIATIONS

ASCM	Agreement on Subsidies and Countervailing Measures
DSU	Dispute Settlement Understanding
EU	European Union
FIT	feed-in tariff
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GPA	Government Procurement Agreement
SPS	Sanitary and Phytosanitary
TBT	Technical Barriers to Trade
TRIPS	Trade-Related Aspects of Intellectual Property Rights
US	United States
WTO	World Trade Organization

INTRODUCTION

This paper examines

- whether and how existing decisions of World Trade Organization (WTO) panels and the Appellate Body have affected (expanded) the policy space for WTO Members to pursue industrial policies under WTO law; and
- how such policy space could be further expanded through WTO panel and Appellate Body decisions.

The paper is structured as follows.

First, the paper presents general conceptual reflections on how WTO dispute settlement can influence the policy space available to WTO Members to adopt industrial policy measures. These conceptual reflections address the role of WTO panels and the Appellate Body in general; the nature and categorization of WTO legal provisions applicable to trade in goods; and the interpretation of categories of rules most likely to impact the policy space of WTO Members.

Second, as specifically requested in the terms of reference, we shall briefly discuss two cases in which the Appellate Body interpreted certain WTO provisions in a manner that arguably creates more policy space for industrial policy measures than alternative interpretative approaches would have permitted.

Third, we will discuss other potential examples of how WTO dispute settlement decisions could create or enlarge policy space under other WTO legal provisions with respect to industrial policy measures.

By way of disclaimer, this paper does not endorse any specific interpretative approach under any particular WTO legal provision. Nor does it advocate greater or lesser flexibility for implementing industrial policies. Rather, it is intended to be an impartial legal-technical analysis, seeking to identify the interpretative levers available to WTO adjudicative bodies, which could be used—intentionally or incidentally—to enlarge the policy space that WTO Members enjoy for implementing industrial policy.

ANALYSIS

CONCEPTUAL REFLECTIONS ON THE IMPACT OF WTO DISPUTE SETTLEMENT ON MEMBERS' 'POLICY SPACE'

The role of WTO adjudicative bodies in general

As a general proposition, the impact of WTO case law on the policy space enjoyed by WTO Members in the field of industrial policy—or in any other policy area subject to WTO rules—will always be severely limited in comparison to the treaty- or rule-making process itself. There are two reasons for this.

First, strictly speaking, WTO case law cannot “expand” or “diminish” the scope of flexibilities that Members enjoy under WTO rules. WTO adjudicative bodies can only interpret legal provisions, so as to discern their true meaning, and apply them to the facts of a case before them. WTO panels and the Appellate Body may not change the rules, create rules where there are none, or subtract from the existing rules.¹ For instance, WTO jurisprudence cannot undo or ignore the prohibition on local content or export subsidies. Rather, only a modification of the WTO rules themselves, through action by the Members as a whole, could bring about such a change. However, WTO case law can clarify, for instance, that certain sets of circumstances or particular types of measures do not give rise to export contingency.

At the same time, WTO law, like any set of legal rules, is not a monolithic block capable of only one reading. It is undisputable that many WTO provisions lend themselves to a range of interpretations, some stricter and some more lenient. This applies, in particular, to inherently vague terms (“reasonable,” “material,” and the like.), or to inherently fact-dependent legal constructs, such as *de facto* export contingency, *de facto* local content contingency, or to the assessment of economic effects in “serious prejudice” disputes under the Agreement on Subsidies and Countervailing Measures (ASCM). Case law will, therefore, occasionally reflect at least some (conscious or sub-conscious) policy preference of the adjudicator. However, these policy preferences will come in many different forms

¹ This is true for any judicial organ. In WTO law, this principle is spelled out explicitly in Article 19.2 of the Dispute Settlement Understanding (DSU), which provides that the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements. Article 3.2 of the DSU stipulates the same rule for the rulings and recommendations of the Dispute Settlement Body, which are of course based on panel and Appellate Body determinations.

and may not be related (only) to the adjudicator's attitude to industrial policy. For instance, an adjudicator's preferences may relate to interpretative techniques (for example, greater or lesser emphasis on textual interpretation or on object and purpose), or concerns unrelated to industrial policy, such as greater attention to environmental or health protection. Finally, from a *realpolitik* perspective, given the ethos prevalent within the broader international trade community, if we do assume that an adjudicator will bring a particular policy preference concerning industrial policy to the table, this may very well be a negative preference. That is, the adjudicator may be skeptical about the legitimacy of measures designed to promote specific national industries, or about encouraging the structural evolution of the economy through measures covered by WTO disciplines.

Second, the impact of any interpretation and application of law is, in principle, only relevant to the dispute at hand and binding only on the parties to the dispute. A universally binding (authoritative) interpretation may only be rendered by the Ministerial Conference, pursuant to Article IX:2 of the WTO Agreement.

This second point, however, must be nuanced. In practice, there is *de facto* precedent in WTO law. The interpretation of a particular provision—once articulated by the Appellate Body—is valid far beyond the confines of an individual dispute.² Moreover, even if a WTO Member's measure is not currently contested before a WTO panel, an interpretation provided in connection with another Member's similar measure will have implications also for the non-disputed measure, potentially increasing the risk that a challenge will occur in the future. Moreover, the interpretation may also have a chilling effect on Members contemplating to promulgate such measures.

How can a particular interpretation or application of the law affect WTO Members' policy space?

Within the limits set out above, we can discern two broad pathways in which dispute settlement interpretations and findings can shape the (real or perceived) policy space of WTO Members in pursuing policies, including industrial policies.

First, interpretation/application of the law may clarify that a particular WTO legal provision has a broader or narrower reach, thereby influencing the domestic rule-making process. For instance, the Appellate Body found in *Canada – Autos* that Article 3.1(b) of the ASCM prohibits not only *de jure*, but also *de facto* local content-contingent subsidies.³ A finding of this type may have a limiting or chilling impact on WTO Members wishing to subsidize domestic producers. When providing subsidies, governments now have to be concerned not only about formally *de jure* local content-contingent subsidies, but also about subsidies that may, in fact, operate in such a manner. Had the Appellate Body espoused the opposite view, it would have allayed those concerns, thereby potentially encouraging WTO Members to grant a broader

range of subsidies, including those that are not explicitly and formally local content-contingent.

Second, a given interpretation and application may encourage or discourage challenges by potential complainants. This second effect may occur as a consequence of the first effect, or independently of it. This may occur in instances in which WTO adjudicative bodies interpret a particular provision in a heavily case-specific manner, signaling to potential future complainants that the next time around, the interpretative approach may be different;⁴ shy away from establishing clear interpretative guidelines, criteria, or benchmarks; shift such benchmarks over time; or when different panels adopt contradictory approaches. Such findings inject a degree of uncertainty and unpredictability into how a provision will be read and applied in a future case, possibly resulting in a chilling effect on potential complainants. WTO Member governments are generally risk-averse in bringing disputes and want to be certain to win. Lack of predictability—created or reinforced by case law—may discourage complainants and encourage regulating WTO Members to take advantage of the reduced likelihood of a WTO dispute.

For instance, in *Canada – Feed-in Tariff Program*, the Appellate Body may have introduced uncertainty with regard to the benefit analysis under Article 1.1(b) of the ASCM. Specifically, it is not clear how the Appellate Body will, in future disputes, distinguish between circumstances in which a government intervenes or distorts an existing market, on the one hand; and circumstances in which the government's intervention is deemed to be so far-reaching as to create a new market, on the other hand. As explained later, this distinction has significant impact on the benefit analysis.⁵ This uncertainty may, *ceteris paribus*, deter some future complainants from bringing subsidy challenges, due to a perception that the benefit analysis has become less predictable, at least in a particular category of subsidies. This might, in turn, at the margin increase the confidence of subsidizing governments

2 Although panel and Appellate Body reports are only binding for the parties to the dispute (Appellate Body Report, *US – Stainless Steel [Mexico]*, para. 158), they also "create *legitimate expectations* among WTO Members, and, therefore, should be taken into account" in subsequent disputes (Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 14, emphasis added). Moreover, the Appellate Body has held that "ensuring 'security and predictability' in the dispute settlement system, ... implies that, absent cogent reasons, an adjudicatory body will resolve the same legal question in the same way in a subsequent case" (Appellate Body Report, *US – Stainless Steel [Mexico]*, para. 160).

3 The Appellate Body in that dispute reversed the panel's ruling that Article 3.1(b) did not apply to *de facto* local content-contingent subsidies. This is an example of how the Appellate Body has narrowed policy space available for WTO Members in matters related to industrial policy.

4 WTO adjudicative bodies often emphasize the case-specific nature of their analysis. See for instance, Appellate Body Reports: *EC and Certain Member States – Large Civil Aircraft*, para. 1376; *Korea – Dairy*, para. 127; *Thailand – H-Beams*, para. 87; *US – Upland Cotton*, para. 277; *US – Softwood Lumber IV*, para. 102; and Panel Report, *US – Export Restraints*, para. 8.76.

5 See the example in Section 2.2.2.

that subsidies in particular areas are less likely to be challenged at the WTO.

By way of another example, there is evidence that the existing—and in my view correct—perception that claims under Article 2.2 of the Agreement on Technical Barriers to Trade (TBT Agreement) are extremely difficult to win is having a deterrent effect on potential complainants pondering whether to bring claims under this provision.⁶

Which category of WTO provisions has the greatest impact on Members' industrial policy space?

In this section, we shall attempt to categorize WTO provisions and enquire which of these categories will typically have the biggest impact on Members' policy space in the field of industrial policy.

Legal nature of WTO provisions on trade in goods

In the field of trade in goods, many WTO provisions fall in the two following categories—prohibitions or restrictions on particular categories of measures; and exceptions to these prohibitions or restrictions.

(i) Prohibitions or restrictions

These provisions limit the discretion of WTO Members on the implementation of domestic legislation. They are negative, or prohibitive in nature, and instruct Members what not to do. Examples include,

- the prohibition to apply import tariffs in excess of the bound levels (Article II:1 of the General Agreement on Tariffs and Trade [GATT] 1994);
- the prohibition to apply quantitative restrictions (Article XI of the GATT 1994);
- the prohibition to grant more favorable treatment to domestic products to the detriment of imported products, including through local content requirements (Article III:4 of the GATT 1994; Article 2.1 of the TBT Agreement; 3.1(b) of the ASCM);
- the prohibition to grant export or local content subsidies (Article 3 of the ASCM); and
- the restriction on granting domestic production subsidies that cause adverse effects to the economic interests of other Members (Articles 5 and 6 of the ASCM).

As long as WTO Members avoid the conduct proscribed or restricted by these provisions, they are free to enact whatever legislation they wish. For instance, they enjoy extremely broad discretion in the implementation of fiscal measures.⁷ WTO Members need not treat all companies, or categories of companies, equally in terms of corporate taxation. However, this discretion ends where tax laws begin

to operate as an export subsidy or discriminate in favour of domestic products. For instance, a reduction in the income tax rate on revenue generated by export sales was found to constitute a prohibited export subsidy in *US – FSC* and *US – FSC* (21.5).⁸

(ii) Exceptions

We can think of exceptions under WTO law in two different ways. First, as exceptions in the strictly legal sense; and second, as legal provisions under WTO law that, although from a legal perspective framed as legal rights, are nevertheless exceptions by their essence or nature.

First, exceptions in the strictly legal sense are a category of WTO provisions that become relevant once a prohibition or restriction has been violated. Exceptions provide a potential justification for WTO-inconsistent measures. The underlying logic of an exceptions provision is that although a measure violates some aspect of WTO law, this violation may be justified because a non-trade policy goal makes the departure from the basic disciplines acceptable.

Qualifying non-trade policy goals include, for instance, protection of public health or public morals, conservation of natural resources, or ensuring the enforcement of other WTO-consistent policies.⁹ For instance, an export restriction found to be in breach of Article XI may ultimately be WTO-compatible because it assists the government in operating a sustainable management scheme for exhaustible natural resources. Similarly, some degree of dissimilar treatment of domestic and foreign enterprises may be justified to ensure effective protection of intellectual property rights.¹⁰

Such exceptions are enshrined, for example, in Articles XI:2, XX and XXIV of the GATT 1994, or the "Enabling Clause."¹¹ Outside trade in goods, one can also mention Article XIV of the General Agreement on Trade in Services (GATS).

An important procedural aspect attaching to these exceptions is that, in a WTO dispute settlement process, they must be actively invoked by the defendant as a "shield"

6 Article 2.2 prohibits technical regulations that, although not discriminatory, are nevertheless unnecessarily restrictive, both for domestic and foreign producers and suppliers.

7 Appellate Body Report, *US – FSC* (21.5), paras 139–140.

8 Panel Report, *US – FSC*, para. 7.130 (subsequently upheld by the Appellate Body in paras. 121 and 177[a] of its report); Panel Report, *US – FSC* (21.5), para. 8.75 (subsequently upheld by the Appellate Body in paras. 120 and 256 [b] of its report).

9 Often, the operation of an exception entails a reversal of the burden of proof, away from the complainant to the defendant.

10 This issue was discussed in the GATT Panel Report in *United States – Section 337 of the Tariff Act of 1930*, paras. 5.31–5.33 (GATT document L/6439, 7 Nov 1989, BISD 36S/345).

against the complainant's challenge. If the defendant does not invoke these exceptions provisions, the panel or the Appellate Body are not permitted to raise and apply these provisions on their own motion.¹² Moreover, the defendant also bears the burden of demonstrating that all substantive conditions for their application have been satisfied.

Second, we turn to certain types of provisions that may be *exceptions in terms of their content or essence*, but not in a formal legal sense. These provisions provide a right for Members to take certain measures and discipline that right. These measures may be challenged by a complainant in a WTO dispute—who also bears the burden of proof—rather than invoked as a defense by a defendant. However, these measures, by their nature, constitute a departure from certain WTO obligations.

For instance, trade remedies are exceptions to the principle of tariff bindings or the prohibition of quantitative restrictions. WTO Members may in principle not exceed their tariff bindings, unless they do so, for example, via anti-dumping measures imposed in accordance with the Anti-dumping Agreement. Similarly, Members may introduce quotas in the form of safeguard measures under the Agreement on Safeguards. However, legally-technically, trade remedies do not operate as “exceptions” in the WTO legal order. Rather, WTO law enshrines a positive right for Members to take/impose trade remedy measures following a domestic investigation. Other Members may initiate WTO dispute settlement proceedings against such measures. These complaining Members then bear the burden of demonstrating any inconsistency with the Anti-dumping Agreement.

(iii) Provisions establishing positive (affirmative) requirements

Finally, WTO law also includes positive rules that require WTO Members to affirmatively take particular regulatory action. A good example are rules related to transparency. For instance, Article X:1 of the GATT requires publication of trade-related legislation. Article X:3(b) requires the creation of tribunals or procedures to enable review of administrative customs decisions.¹³ However, such rules are not as common in the goods area as they are, for instance, under the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). In any event, these provisions are not central to the subject of this paper.¹⁴

Which category of provisions will likely have the greatest impact on industrial policy space?

Drawing on our categorization in the preceding section, which categories of measures will be the main “battlefield” on which the policy space of Members for industrial policy may be influenced through dispute settlement?

Arguably, most flexibilities flowing from WTO case law will result from the interpretation and the application of

prohibitions or restrictions. The relevant findings under those provisions could clarify that a particular measure does not fall under a given provision at all; alternatively, even if the measure falls under the provision, that it does not violate the rule contained in that provision. In contrast, I would submit that the interpretation of provisions that enshrine exceptions (in the strict legal sense, that is, the first type identified above) will likely play a limited role in this regard.

For instance, WTO case law can clarify what constitutes a subsidy by interpreting and applying a broader or narrower concept of “financial contribution” under Article 1.1 of the ASCM. A broader reading of the definitional term “financial contribution” will capture a broader range of domestic measures and subject them to WTO subsidy rules. A narrower reading of the same term will reduce the universe of domestic measures captured by WTO law.

A number of other prohibitive or restrictive provisions under the ASCM can also be interpreted in ways that expand or limit the policy space of WTO Members. For example, WTO case law can provide greater policy space for Members by interpreting and applying in a stricter manner the provisions of Articles 5 and 6 of the ASCM, pursuant to which Members can demonstrate that another Member's subsidies have caused “adverse effects” to their economic interests. Similarly, where a Member challenges particular domestic pricing policies—for instance, minimum or maximum price regulation—as a non-tariff import restriction under Article XI, a WTO panel will have to decide whether the measure at hand falls within the scope of the prohibition under Article XI.

11 Article XI:2 is an exception from the application of the prohibition enshrined in Article XI:1 (“no prohibition or restriction ... shall be instituted ... on the importation of any product”). Hence, a quantitative restriction is permitted if it falls within the scope of any of the three paragraphs or Article XI:2 (for example, Article XI:2[a] which refers to “export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs”). See Decision on Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries (GATT document L/4903, 28 Nov 1979, BISD 26S/203).

12 Rather incomprehensibly, the Appellate Body has found with respect to the Enabling Clause that the complainant bears the burden of “raising” it. It remains unclear to this date what precisely this means and how it fits in the usual allocation of the burden of proof in WTO dispute settlement (Appellate Body Report, *EC – Tariff Preferences*, para. 118).

13 As another example, the TBT Agreement and the Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures require the creation of “enquiry points” to enable traders easily to obtain information about applicable sanitary and technical regulations (Annex B[3] of the SPS Agreement and Article 10 of the TBT Agreement).

14 Provisions dealing with transparency and institutional aspects contribute to good governance, which will have a positive impact on the overall business and investment environment. However, beyond these general (and no doubt very important) aspects, these provisions are not relevant to industrial policy in the sense of targeting eligible industries for greater development, fostering structural adjustment of the national economy, or ensuring greater integration of the domestic industry in transnational value chains.

In contrast, case law interpreting and applying exceptions (most prominently, Article XX of the GATT 1994) in my view holds much more limited promise for defining and introducing flexibilities for industrial policy.

There are two fundamental reasons why exceptions provisions are less important in this regard.

First, industrial policy per se—that is, the support for domestic industries at least in part because they are domestic—is not recognized as a public policy worthy of reprieve from the strictures of WTO rules. For instance, neither Articles XX nor XI:2 of the GATT 1994 refer to industrial policy, support for domestic industry, or measures to ensure structural adjustment of the economy as valid regulatory goals that justify overriding the disciplines of WTO law. Similarly, it is unlikely that such regulatory goals would be included among the legitimate regulatory objectives that the Appellate Body has read into Articles 2.1 or 2.2 of the TBT Agreement.

Quite to the contrary. Many of the fundamental WTO rules have historically been drafted to prevent WTO Members from protecting their domestic industry at the expense of, and to the exclusion of, foreign producers or traders. For instance, prohibitions on discrimination under Article III of the GATT 1994, or the prohibition of export subsidies under Article 3.1(b) of the ASCM, were created precisely to prevent such policies.

Admittedly, this assertion has to be qualified. In some very specific (but rather rare) circumstances, the goal of protecting domestic industry or fostering an infant industry is explicitly enshrined as legitimate grounds on which to justify the departure from WTO disciplines. For instance, Article XVIII:C and XVIII:D of the GATT 1994 entitles developing countries to take WTO-inconsistent measures to foster infant industries, subject to procedural authorizations by the General Council.¹⁵

Another qualification is that the application of WTO-consistent measures, in the pursuit of WTO-legitimate public policy goals other than industrial policy, could, as an indirect consequence, also increase the margin for industrial policy. For instance, assume that a Member creates a CO₂ “cap-and-trade-regime” and imposes a WTO-compliant carbon offset tax on imported goods. This offset tax could be WTO-consistent because it does not result in any discrimination. It could also be WTO-consistent because, although placing imports at a disadvantage, it is justified under Article XX(b) or XX(g) as necessary for environmental purposes. Such a WTO-consistent/justified offset scheme might result in shifting domestic demand to the (clean) domestic industry and thereby economically benefit that domestic industry. However, if the offset tax was deliberately created ex ante with the goal of shifting demand away from foreign suppliers to the domestic industry (whether alone or together with bona fide environmental concerns), this intention will likely be discernible from the structure or the operation of the

measure. This, in turn, will make it highly unlikely that such a measure would survive a WTO challenge. A WTO panel or the Appellate Body would likely separate out the portions of the measure driven by the intent to benefit the domestic industry, and would find them WTO-inconsistent and require their elimination or adjustment.

A good illustration of this point are domestic laws that both promote the use of green energy and simultaneously stipulate local content rules as conditions for eligibility.¹⁶ The local content aspect is separable from the ecological aspect, and is easily challengeable under existing WTO rules. Once such a measure has been found to violate WTO law—for example, Article III:4 of the GATT 1994—it will be next to impossible to justify that measure under Article XX of the GATT 1994.

A loosely related example is also the application of strict technical product and environmental standards under the TBT and SPS Agreements. WTO Members are expected to follow internationally agreed standards, where these exist, but may opt for their own higher levels of protection. These high national technical standards may—even if WTO-consistent—act as significant trade barriers, for instance, for producers from developing countries. The trade-related impact of these standards cannot be underestimated. It is likely to become an even more prominent trade barrier in the years to come, also due to the proliferation of “private standards,” that is, product specifications imposed by private market actors (for example, large retailing chains). As a consequence of high technical standards, the local industry may be shielded to a certain extent from competition from at least some or even the majority of foreign suppliers. Thus, WTO-consistent action covered by the TBT and SPS Agreements may have an indirect impact on and benefit the domestic industry.

Nevertheless, if Members actively and deliberately pursue targeted industrial policies—fostering structural adjustment of the national economy or seeking to ensure its greater market share—through high product or environmental standards, they may run afoul, for instance, of the prohibition under Article 2.2 of the TBT Agreement and 5.6 of the SPS Agreement. Under these provisions, national

¹⁵ As another example, trade remedy measures may be imposed to provide relief to struggling domestic industries or protect industries in the process of establishment, provided certain substantive and procedural conditions are met. One could argue that the conceptual underpinning of such measures is not industrial policy, but rather the protection of industry from unfair trade or unexpected import surges. In practice, however, WTO Members do occasionally see trade remedies as a complement to a broader policy of fostering and providing protection to particular domestic industries.

¹⁶ There are three cases to date where such measures have been challenged at the WTO—*Canada – Feed-in Tariff Program* (DS412, 426) (complainants: the European Union [EU] and Japan); *European Union and Certain Member States – Certain Measures Affecting the Renewable Energy Generation Sector* (DS452) (complainant: China); and *India – Certain Measures Relating to Solar Cells and Solar Modules* (DS456) (complainant: the United States [US]). The latter cases appear to be still at the stage of consultations.

measures may be found to be more trade restrictive than necessary to achieve the legitimate policy objectives stipulated in those agreements, such as product safety, environmental protection, or public health.

The second reason why the interpretation of exceptions by WTO panels and the Appellate Body is unlikely to enlarge policy space for industrial policy is rather straightforward. A number of restrictions/prohibitions provided for in WTO agreements are not mitigated or balanced by an exceptions provision. For instance, a violation of the prohibition of export subsidies or of local content subsidies—in Article 3.1 of the ASCM—cannot be justified under an exceptions provision because the ASCM does not include such exceptions. There is a lively debate as to whether Article XX of the GATT may be applied under other goods agreements under Annex 1A, but recent Appellate Body case law strongly suggests that this will typically not be the case.¹⁷ Hence, once a measure is found to constitute an export subsidy or a local content subsidy, it will be WTO-illegal and not amenable to justification under an exceptions provision.

TWO EXAMPLES OF WTO CASE LAW THAT LIKELY EXPANDED THE POLICY SPACE FOR MEMBERS' INDUSTRIAL POLICIES

This section illustrates how an interpretation and application of existing WTO rules by WTO dispute settlement bodies has potentially or actually expanded industrial policy space for Members.

Interpretation of the de facto export subsidy standard under Article 3.1(a) of the ASCM in *EC – Large Civil Aircraft*

The first example is the interpretation and application of the de facto export subsidy standard under Article 3.1(a) of the ASCM. To recall, Article 3.1(a) prohibits WTO Members from granting subsidies that are in law or in fact (de facto) contingent on export performance.¹⁸ De facto contingency can be very complex to assess because it will be based on a configuration and a holistic assessment of a range of facts of the specific case. The rule maker (legislator) cannot specify the parameters of such rules in advance. This means that the interpretative approach, as well as the weighing and balancing of facts in any given case, must be chosen by the adjudicator. As a result, the adjudicator will have a pronounced impact on how strictly or leniently this particular norm will operate in practice.

Relatively recently, in *EC – Large Civil Aircraft*, the Appellate Body clarified the de facto export contingency standard in a manner that may provide greater scope for industrial policies of WTO Members. The Appellate Body had interpreted that standard on previous occasions, but its findings arguably lent themselves to diverging interpretations. Building on

that previous case law, the panel in *EC – Large Civil Aircraft* found, in essence, that the de facto standard was met where the motivation behind a granting authority's decision to subsidize lies in its expectations that exports will ensue. On that reading, the de facto contingency appeared to be at least to some extent linked to an authority's (subjective) expectations. This suggested that a complainant would have to prove that the granting authority was aware that the recipient would export on, or in anticipation of, receipt of the subsidy; and that this anticipation of the government was (one of) the reason(s) why it granted the subsidy.

Although this panel interpretation was not an implausible reading of the Appellate Body's earlier findings, the Appellate Body in *EC – Large Civil Aircraft* reversed it and articulated a standard that arguably leaves more margin of maneuver for subsidy-granting WTO Members. Specifically, it held that the test for establishing de facto export contingency is whether the granting of the subsidy is "geared to induce the promotion of future export performance by the recipient" (para. 1044). This clarified standard would be satisfied where the subsidy gives the recipient the incentive "to export in a way that is not simply reflective of the conditions of supply and demand in the domestic and export markets undistorted by the granting of the subsidy" (para. 1045).

Thus, the standard of de facto export contingency would be satisfied where the ratio of exports to domestic sales would be skewed in favor of exports. For instance, where the industry previously exported half (50 percent) of its production, a subsidy would be de facto export contingent if it induced the industry to export two-thirds of its production. In contrast, if the subsidy recipient increased both its export and domestic sales in absolute terms, but the ratio between the two remained unchanged (50:50), no export subsidy would exist and Article 3.1(a) would not be infringed (paras. 1047, 1048). Moreover, although the Appellate Body did not say so, one can speculate that even a relative increase in export sales post-subsidy (for example, 60 percent vs. 40 percent) may not run afoul of Article 3.1(a) if the subsidizing member could demonstrate that this relative increase of exports (from 50 percent to 60 percent) was not a consequence of the subsidy, but rather of, for example, higher international demand while demand in the home market was stagnant or declining.

Reactions from the trade community to the Appellate Body ruling differed. Some commentators argued that the Appellate Body had established a new standard; others felt that it had merely clarified its previous rulings, which in turn reflected a straightforward reading of Article 3.1(a) of the ASCM.

¹⁷ This recent case law includes cases such as DS363, *China – Publications and Audiovisual Products*; DS398, *China – Raw Materials*; DS433, *China – Rare Earths*; and DS406, *US – Clove Cigarettes*.

¹⁸ By way of an exception, export subsidies may be granted for agricultural products to the extent that the right to do so has been reserved by the individual WTO Member in its goods schedule.

Assuming that the Appellate Body's ruling may have some impact on domestic policies, its implication for industrial policy may be two-fold. First, the interpretation may signal greater substantive leeway for WTO Members to grant subsidies that give rise to exports. They may provide subsidies even where they know or anticipate that these subsidies will lead to greater exports, and even if these increased exports are a (subjective) motivation for the government to grant the subsidies. For instance, a WTO Member may promote international sales of a domestic industry to better integrate it in international value chains as long as the subsidy is not explicitly export-contingent and as long as the Member is confident that domestic sales will grow in tandem with exports.

Second, complainants may be somewhat more reluctant to initiate complaints under Article 3.1(a) because they may be required to adduce data demonstrating that the ratio of exports to domestic sales has been skewed through the subsidy. Moreover, if a subsidy programme is newly introduced, the complainant may need to wait to assemble a range of reliable empirical data covering a few years.

Nonetheless, it should be noted that the subsidies at issue, even if no longer caught by Article 3.1(a) of the ASCM, remain actionable and countervailable if they cause "adverse effects" to the interests of another Member in its home market, in the market of the subsidizing country, or in third country markets.¹⁹ Put differently, an absolute increase in export sales due to a subsidy does not violate Article 3.1(a) as long as the relationship between domestic and export sales is not artificially skewed by that subsidy. However, this absolute increase may give rise to successful claims under Articles 5 and 6 of the ASCM if the additional export sales crowd out sales that would have otherwise been made by other Members' companies. Nevertheless, "adverse effects" challenges at the WTO are more complicated and more challenging due to the need to provide empirical economic evidence. Such challenges are, therefore, less frequent in the WTO than challenges to export subsidies.

Finally, WTO Members may apply countervailing duties to subsidized exports. However, doing so will only protect their own markets and not address any lost sales or any price effects that the subsidies may have in third country markets or in the subsidizing Members' home markets. Moreover, countervailing duties create no obligation on the subsidizing Member to withdraw the subsidy or remove its effects.

All in all, the implication of the Appellate Body's ruling in *EC – Large Civil Aircraft* is likely a net increase in policy space for subsidizing WTO Members.

Interpretation of the benefit benchmark under Article 1.1(b) of the ASCM in Canada – Feed-in Tariff Program

The second example is the interpretation of the "benefit" requirement under Article 1.1(b) of the ASCM in the *Canada – Feed-in Tariff Program* case.

By way of background, pursuant to Article 1, a subsidy is defined as a "financial contribution" granted by a government and conferring a "benefit" to the recipient. If the subsidy is specific to (that is, "targets") certain industries or enterprises, it is subject to the disciplines of the ASCM.²⁰ In other words, the disciplines on domestic subsidies will apply only to measures that meet the definitional elements of a subsidy, as provided under Article 1 and that are specific. Subsidies that do not meet these criteria are not subject to the WTO's subsidy disciplines. Therefore, a narrower interpretation of the constituent elements of a subsidy limits the reach of the WTO subsidy disciplines and increases the universe of measures falling outside the disciplines of the ASCM.²¹

The *Canada – Feed-in Tariff Program* case concerned a so-called feed-in tariff (FIT) program implemented by the province of Ontario, Canada. The program was designed to promote the generation of electricity from renewable sources, such as wind, solar, or water power. It guaranteed a minimum price to generators of renewable electricity. The need for such special programs arises because generators of renewable electricity face high production costs and cannot compete on price with generators of conventional energy. Therefore, absent government intervention, electricity markets would typically fail to attract the necessary investments for building generation capacity for renewable electricity.

To qualify for participating in the FIT program, Canada required electricity producers to use generation equipment (for example, wind turbines) with a certain minimum local content requirement. This aspect was the reason behind the challenge by the European Union (EU) and Japan, who argued, *inter alia*, that the program constituted a prohibited local content subsidy and a prohibited trade-related investment measure.

In their claims under the ASCM, the EU and Japan argued that the guaranteed price for electricity was a financial contribution; that the guaranteed price conferred a benefit

¹⁹ See Part III and Part V of the ASCM. However, in such situations a complainant would have additional hurdles to surpass, such as showing "specificity," on one hand, and "injury" to the domestic industry, "nullification or impairment" of benefits, or "serious prejudice," on the other hand.

²⁰ If a subsidy is export contingent or contingent on the use of imported over domestic goods, it is deemed to be specific.

²¹ Of course, other WTO agreements may still apply to those measures.

because it was above prevailing (conventional) energy market prices; and that this subsidy was conditioned on the use of local over imported equipment. The second of these three questions became the key battleground during the proceedings. Did the guaranteed price paid to the FIT generators confer a benefit to those generators, that is, made them better off than on the free market? How does one conduct the benefit inquiry in a highly regulated, sui generis market such as the electricity market? What is the benchmark to measure the guaranteed price against?

One can envisage several distinct approaches to this question. First, the mere fact that FIT generators exist and are able to operate in a market where they would otherwise find it impossible to operate, absent the governmental support programs, is sufficient on its own for a finding that a benefit has been conferred. Let us label this approach "Approach 1." Approach 1 is rather sweeping and does not require any particular numerical market rate as a benchmark to measure the guaranteed price against.

As a second, alternative approach, one can compare the price paid to FIT generators with the price for electricity observable in the "market" for electricity. The relevant "market" could be the entire electricity market, that is, conventional and renewable energy taken together (Approach 2a), or the market only for renewable electricity (or for each type of renewable energy separately) (Approach 2b).

As one moves along this spectrum of approaches, from Approach 1 to Approach 2b, the identification of the market benchmark and/or of benefit becomes more difficult. This arguably expands the policy space for the regulating government because it complicates the finding that a subsidy exists. Under Approach 2b, the identification of the benchmark and ultimately of benefit itself is particularly difficult, because the "market" will have been created by governmental intervention and be permeated by government regulation. This may deter or, at the very least, complicate a WTO challenge.

The panel in this dispute chose Approach 2a, whereas a dissenting panelist chose Approach 1.²² The Appellate Body opted for Approach 2b. It rejected both Approach 1 and 2a. Underlying the rejection of both these approaches was the premise that renewable electricity was sufficiently distinct from conventional electricity to form a separate market (and indeed that wind and solar power, respectively, formed two separate markets). The distinction drawn by the Appellate Body between conventional and renewable electricity, and their separation into two distinct markets, was largely driven by supply side aspects, in particular differences in production costs.

The Appellate Body thus opted for Approach 2b. Crucially, it ruled that a market newly created by the government cannot automatically be deemed to be distorted and cannot be measured against a benchmark (proxy) taken from another geographical market—although this is precisely

what previous case law would have suggested. If one were to use such a proxy benchmark, it would automatically lead to false positive findings of benefit. Rather, the Appellate Body instructed panels to seek to identify, within the market newly created by the government, the price that "a hypothetical market would yield." This is because, according to the Appellate Body, even in a government-created market, market forces may find sufficient space to operate (para. 5.228). It then suggested several ways in which to discover such a hypothetical market price in the Canadian case.²³ Ultimately, the Appellate Body was unable to reach a conclusion for lack of sufficient facts.

The following appears to be most relevant from an industrial policy perspective. The Appellate Body's ruling in *Canada – Feed-In Tariffs* has essentially re-qualified a government's effort to make a (new) product competitive with another, established product. The Appellate Body considered this government action as the creation of a new market, rather than—as prior case law would have suggested—as an intervention in and distortion of an existing market. Unlike the panel's analysis, the Appellate Body's findings are—at least on their face—not limited to electricity markets. Qualifying a governmental policy as the creation of a new market makes the benefit analysis more demanding and less predictable, thereby complicating multilateral challenges as well as the imposition of countervailing duties. This enlarges the policy space of intervention-minded WTO Members. Indeed, it was arguably the Appellate Body's intention to inject legitimate policy considerations—such as environmental concerns—into the benefit analysis.²⁴

The Appellate Body's ruling thus appears to provide more policy space for, or make less likely challenges of, environmentally motivated measures. We could think of, for instance, measures intended to promote eco-friendly products or services, such as environmental-friendly transport, low-emission production methods, and products produced by such methods. For instance, if a government provides preferential loans to industries for environmentally friendly, but more costly production technologies, could the government be said to be creating a new market for (loans for) these technologies? If yes, this would presumably make it more difficult to identify the appropriate benefit benchmark—for example, the interest rate for such loans might no longer be measured against the generally prevailing interest rate to assess benefit. Rather, the preferential rate

22 | Nevertheless, the panel found the actual market data at hand distorted due to strong governmental intervention and sought to identify "out-of-country" benchmarks, in keeping with previous Appellate Body case law.

23 | The Appellate Body mentioned in this regard—the methodology used to determine the administered price; administered prices for the same product in other markets; or a price-discovery mechanism such as competitive bidding or negotiated prices.

24 | Moreover, it is not clear whether a cost plus rate of return benchmark is (always) consistent with the outcome in competitive markets, as the Appellate Body appeared to assume.

would have to be measured against another benchmark that would reflect the “hypothetical market outcome” in the new market.

Nevertheless, it is doubtful that this new type of benefit analysis will become generally applicable. The Appellate Body’s undisclosed goal in the *Canada – Feed-In Tariffs* was to provide policy space for environmentally motivated measures, or at the very least for renewable energy policies. The Appellate Body’s new approach would probably not permit “pure” industrial policy goals to influence the benefit analysis. For instance, providing support to the domestic steel industry, or a sub-segment of the domestic steel industry, simply for the purpose of providing an advantage over foreign competition is highly unlikely to result in the creation of a new market. Nevertheless, environmental or other policies, rendered less challengeable through this new line of case law, could have indirect industrial policy-relevant impacts.

OTHER EXAMPLES OF HOW WTO CASE LAW COULD INCREASE POLICY SPACE FOR INDUSTRIAL POLICY MEASURES

We have just seen two examples of how WTO adjudicative bodies have interpreted a WTO provision in a manner that may increase the policy space for Members to pursue industrial policies. At the very least, these interpretations complicate a WTO challenge and may deter other Members from bringing such challenges in the first place. In either scenario, all things being equal, we could expect greater use of industrial policy measures.

In this last section, we shall consider other examples of how decisions of the WTO judiciary could bring about similar effects through interpretation and application of WTO provisions.

Import/export measures

Tariffs

As is well known, WTO Members may use tariffs within the scope of their respective tariff bindings. To the extent that the bound levels allow it, even very high tariffs are WTO-consistent. In technical parlance, these tariffs are called “ordinary customs duties” and are distinguished from “other [import] duties and charges.” This latter category has historically comprised charges such as, for instance, temporary customs surcharges, variable import levies, and minimum import prices.²⁵ The dividing line between “ordinary customs duties” and “other duties and charges” is not defined in the treaty text, and case law has struggled to come up with a workable distinction in the abstract.²⁶ Nevertheless, this distinction is important because recourse to ordinary customs duties—within the bound levels—is permitted,

whereas the recourse to “other duties and charges” is subject to very strict conditions.

An example of “other duties and charges” are the so-called variable levies, that is, periodically changing tariffs. These levies are used to “stabilize” domestic prices in the face of volatile international prices and thereby to protect the domestic industry (and to a lesser extent domestic consumers). However, these variable levies are prohibited outright under the Agreement on Agriculture, and their application to non-agricultural products is permitted only subject to the usual disciplines on other duties and charges.²⁷ At the same time, ordinary customs duties (“normal” tariffs) may legitimately be subject to some variation over time, by discrete governmental decisions, as long as they remain within the bound levels. The precise dividing line between a permissible and an impermissible tariff variation has been drawn to some extent, but not exhaustively.²⁸ If WTO panels and the Appellate Body were to permit significant variation in a border charge without classifying this charge as an “other duty and charge,” this would provide greater scope for protection of domestic industry. For instance, WTO Members could protect infant industries from world market price fluctuations, imposing greater tariffs during periods of low international prices and lesser tariffs during periods of higher world market prices.

Quantitative restrictions

WTO law is fairly strict with respect to quantitative (or non-tariff) restrictions under Article XI of the GATT 1994. The case law has adopted a rather broad concept of what constitutes an Article XI violation, far beyond the classic cases of import or export quotas or outright import or export prohibitions. In essence, any measure having a “limiting

²⁵ Article II:1(b) of the GATT 1994.

²⁶ “Other duties and charges” belong to a residual category that includes all duties and charges that are not “ordinary customs duties,” while the latter category “refers to duties collected at the border which constitute ‘customs duties’ in the strict sense of the term” (Panel Report, *Dominican Republic – Safeguard Measures*, paras. 7.79, 7.85). The Appellate Body has found that the form that a duty may take, be it specific or *ad valorem*, is not determinative to the classification of a duty. Nor is it decisive that the calculation of the duty depends on exogenous factors, “such as the interests of consumers or domestic producers” (para. 7.84, citing Appellate Body Report, *Chile – Price Band System*, paras. 216, 217–278).

²⁷ That is, “other duties and charges” may be imposed only if they are recorded in a WTO Member’s goods schedule. Their previous recording in the schedule was moreover subject to additional rules, for instance, that the level of such “other duty and charge” shall not be higher than the level obtaining at the time of the first incorporation of the concession in the schedule.

²⁸ The *Chile – Price Band System* and *Chile – Price Band System* (21.5) disputes have clarified that where variation is caused by a mathematical formula embedded in the legislation, the resulting charge is not an ordinary customs duty (Appellate Body Report, *Chile – Price Band System*, para. 233). However, a duty could be a variable import levy even in the absence of mathematical formulas. See also the recent panel report in *Peru – Agricultural Products* (DS457), unambiguously confirming the *Chile – Price Band System* case law.

effect" or constituting a "limiting condition" on imports can be caught.²⁹ For instance, a restriction on the access of imports to only two designated ports of entry was found to constitute a "limiting condition" in violation of Article XI.³⁰ As another example, a GATT panel report found that certain discriminatory marketing practices by state-related monopolistic distributors constituted Article XI breaches.³¹ Similarly, fines levied on the importation of retreaded tires were also held to be in breach of Article XI, even though they "d[id] not per se impose a border restriction on importation, but rather act[ed] as a disincentive to importation."³²

The universe of other measures that may give rise to some form of a "limiting condition" is potentially vast. For instance, WTO bodies have not determined whether minimum or maximum domestic prices, or certain types of packaging requirements or packaging prohibitions, are covered under Article XI (or under any other WTO provision). If WTO adjudicatory bodies were to clarify that such measure do not give rise to Article XI-type restriction, this could give rise to greater legal certainty for WTO Members to pursue industrial policy goals through such measures, for example, supporting a fledgling domestic industry by guaranteeing a minimum return through a sufficiently high minimum price.

Another example worth mentioning in this context is Article XVIII of the GATT 1994, notably Articles XVIII:A, XVIII:C, and XVIII:D. These provisions enable developing countries to take certain measures to benefit infant industries. Article XVIII:A establishes special rules under which the General Council can authorize the withdrawal of tariff concessions (as an alternative to Article XXVIII) by developing WTO Members with "low standards of living" and at "early stages of development." Article XVIII:C envisages action by the General Council to permit the same developing WTO Members to take measures inconsistent with GATT provisions (other than Articles I, II and XIII)—thus, most typically, import restrictions or outright import bans. Article XVIII:D envisages the same type of action as Article XVIII:C, by authorization of the General Council, for developing countries at a higher level of development than those under Sections B and C.

Articles XVIII:C and XVIII:D are interesting because they are the very rare type of WTO provisions that legitimate otherwise WTO-inconsistent measures taken for purely industrial policy purposes. The relevant requirements are essentially procedural; the use of such measures ultimately depends on authorization by the WTO membership. However, the procedures are very complicated. Perhaps this, together with the requirement to compensate other Members, is one of the reasons why these provisions have been rarely relied on since 1947.³³ Moreover, there does not appear to be much room for WTO adjudicative bodies to add or to subtract from the freedom that Members enjoy under these provisions due to their procedural nature and the fact that the ultimate decision lies in the hands of the General Council.

Trade remedy measures

Trade remedies (anti-dumping and countervailing duties, price undertakings, and safeguard measures) offer countless opportunities for panels and the Appellate Body to provide leeway for Members to apply WTO-consistent measures that benefit domestic industry. Given that both developed and developing countries are users of trade remedies, the significance of this issue cuts across the entire WTO membership.

WTO case law on trade remedies revolves around the question of whether an investigating authority has correctly investigated all relevant facts on the record and correctly determined that the conditions for applying a given trade remedy have been satisfied. These investigations cover a broad range of substantive and procedural aspects. It is beyond the scope of this paper to identify the many ways in which WTO adjudicative bodies can provide greater or lesser margin of discretion to Members' investigating authorities.

Nevertheless, by way of example, we can mention two of the most interesting among the many anti-dumping issues currently pending before the WTO. First, the EU is facing a challenge to its "cost adjustment" methodology.³⁴ Specifically, in calculating cost benchmarks or constructed normal value, the EU occasionally replaces actual input costs that were correctly recorded in the exporters' financial accounts with different, higher figures. It will do so when it considers that another WTO Member's policies lower the market price on that Member's internal market. An example of such measures is an export restriction that results in greater domestic supply of the product, thereby lowering the price at which investigated exporters purchase inputs. This calculation methodology leads to higher dumping margins or creates them in the first place. The EU thereby essentially penalizes foreign companies for their home government's actions (including industrial policy measures) that, in its view, result in objectionable distortions in that country's domestic

29 | Panel Report, *Colombia – Ports of Entry*, para. 7.233–235.

30 | Panel Report, *Colombia – Ports of Entry*, para. 7.25.

31 | GATT Panel Report, *Canada – Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies*, para. 4.25 (GATT document L/6304, 22 March 1988, BISD 35S/37).

32 | The fines were levied on importation, marketing, transportation, storage, and keeping or warehousing of retreaded tires. Panel Report, *Brazil – Retreaded Tires*, paras. 7.370–7.373.

33 | Or the right of other Members to suspend equivalent concessions. For instance, action under Article XVIII:A has been taken only in nine instances since 1947. Action under Article XVIII:C has been taken only 15 times since 1947, of which only three have been since the creation of the WTO.

34 | *European Union – Anti-Dumping Measures on Biodiesel from Argentina* (DS 473); *European Union – Anti-Dumping Measures on Biodiesel from Indonesia* (DS 480); *European Union – Cost Adjustment Methodologies and Certain Anti-Dumping Measures on Imports from Russia* (DS474).

market. The EU will adopt this approach even if these export restrictions are WTO-consistent (for example, export restrictions by means of WTO-legal export duties instead of quantitative export restrictions).

If the WTO adjudicative bodies in the currently pending disputes agree that this methodology is in principle acceptable, this may materially increase Members' ability under WTO law to apply (higher) anti-dumping duties. It may also have a potential chilling effect on those exporting Members who wish to operate export restrictions, including for industrial policy purposes—which seems to be the ultimately intended policy effect of the EU's methodology. Logically, the reverse interpretation by WTO panels and the Appellate Body would limit the scope of discretion for Members to apply (higher) anti-dumping duties in such circumstances; it would also provide the exporting Members with greater certainty that their export restrictions will not result in (higher) anti-dumping duties in key export markets.

A second example is "targeted dumping," a term that by extension refers to a particular way of calculating dumping margins.³⁵ Here, the United States (US) is on trial for its recently vastly expanded use of a methodology that seeks to identify, and respond to, targeted dumping. This methodology that is more likely to result in affirmative dumping findings than would otherwise be the case. This is the case because the US—like other countries that have recourse to "targeted dumping" methodologies—applies the notorious "zeroing" methodology. The use of this methodology has been ruled WTO-inconsistent in a range of circumstances, both in initial investigations and in reviews. However, the current disputes relate to zeroing in a context and under a comparison methodology that has not previously been addressed comprehensively by panels and the Appellate Body. Should the WTO adjudicative bodies rule that the zeroing methodology is (exceptionally) WTO-consistent in the context of "targeted dumping," and take a similarly permissive attitude on other elements of the US' calculation methodology,³⁶ this would materially expand importing Members' ability to apply anti-dumping measures or charge higher anti-dumping duties.

Nevertheless, by way of concluding our remarks on trade remedies, one may question to what extent trade remedy measures should be regarded as part of the tool box of industrial policy measures. On the one hand, trade remedies are industrial policy measures in a very general sense because they are intended to protect a domestic industry, whether it be protection against trade practices labeled as "unfair" (anti-dumping and countervailing measures) or against unexpected surges in imports (safeguards). Moreover, the concept of "material injury" in the anti-dumping and countervailing context also includes "material retardation of the establishment of such an industry."³⁷ This suggests that anti-dumping and countervailing measures can be tools for protecting infant industries and ensuring that the path towards structural industrial transformation is not disrupted by "unfair" trade practices.

At the same time, trade remedies do not entirely fit into the picture of (modern) industrial policy measures to the extent that industrial policy is defined as a deliberate ex-ante pro-active policy to foster modern, future-oriented, high-value added industries and to integrate these industries in global value chains. First, trade remedy measures are—at the very least by their initial design—intended to be reactive to circumstances that arise independently of the regulating government's volition. At least by design, they do not reflect ex ante deliberately conceived industrial policy in the same manner as, for example, a governmental decision systematically to promote a particular industry via subsidies. Of course, in practice, trade remedies may be (ab) used for such a purpose and imposed systematically to shield targeted sectors from foreign competition. Second, remedies are in practice often used to protect relatively mature and typically inefficient industries, such as steel and chemical producers, plastics and rubber or textile products—hardly the sort of future-oriented high-value added industries that a government would actively promote under the rubric of structural transformation of the national economy.³⁸ Moreover, by providing such mature industries with a new lease of life, trade remedy measures may actually delay the kind of structural transformation that is often the very goal of successful industrial policies.

Subsidies

Subsidies are a very common tool of industrial policy and an area in which tension between policy space and legal disciplines may arise frequently. As the two leading examples of this paper in Section 2.2 demonstrate, WTO adjudicators can through their interpretation influence the scope of discretion that regulating Members have in this regard.

Definition of a subsidy

WTO adjudicators can adopt interpretative approaches that shape the definition of subsidies under WTO law. For instance, the case law has taken the view that measures that do not reflect a direct transfer of economic resources—in the sense of a direct flow of economic resources from the government (or a body attributable to the government) to a private recipient or the foregoing of revenue owed—

³⁵ Correctly said, targeted dumping is short-hand for a particular dumping pattern, attributed to the (often entirely unsuspecting) exporter. The targeted dumping comparison methodology, or "third methodology" under Article 2.4.2, is the investigating authority's methodology of calculating the dumping margin in these circumstances.

³⁶ For instance, the precise circumstances in which "targeted dumping" may be considered to arise.

³⁷ Footnote 9 of the Anti-dumping Agreement and footnote 45 of the ASCM.

³⁸ There are of course numerous exceptions. For instance, the EU recently sought to impose anti-dumping measures on solar panels from China, ostensibly to protect its solar panel producers (see Council Implementing Regulation No. 1238/2013).

do not amount to a financial contribution within the meaning of Article 1.1(a)(1) of the ASCM. This holds true even where governmental action, through its economic effects, ultimately has the same effect as would arise from the transfer of money or other transfers of economic resources. By way of example, export duties—which, unlike quantitative export restrictions or export bans, are typically WTO-consistent—that limit exports of raw materials that serve as input for an exporting industry and thereby lead to lower prices on the domestic market, have been ruled not to constitute a financial contribution.³⁹ This means that such measures cannot constitute subsidies and are not subject to WTO (subsidy) disciplines. This arguably expands the scope of action for Members, in that they can promote greater value-added industries on their territory by restricting the export of raw materials.⁴⁰

As shown in the *Canada – Feed-in Tariff Program* example, a more exacting standard for demonstrating benefit may also provide greater policy space for subsidizing members.

Prohibited subsidies

Our example in the *EC – Large Civil Aircraft* case shows that the interpretation and application of the de facto export contingency standard may provide greater margin of maneuver for a subsidizing Member. The same may hold for the de facto local content standard. So far, there has been no finding applying a de facto local content standard. If such a dispute were to occur, WTO panels and the Appellate Body could adopt a relatively lenient approach that would make governments less concerned about granting relevant subsidies. Alternatively, panels and the Appellate Body could adopt an approach that is very case specific and yields somewhat unpredictable case-specific results, thereby potentially dissuading potential complainants from pursuing related disputes. In both instances, this would result in relatively greater discretion for the subsidizing/regulating Member.

For instance, one could envisage an approach analogous to that under Article 3.1(a), the export subsidy prohibition, as clarified by the Appellate Body in *EC – Large Civil Aircraft*, as previously discussed in Section 2.2.1. This approach would stipulate that where the granting of a subsidy was indeed motivated by a government's expectation of greater use of domestic inputs, the de facto local content contingency standard would not be met and Article 3.1(b) would not be violated even if the subsidy recipient purchased more domestic inputs, as long as the subsidy did not skew the ratio between domestic and imported input purchases.

Actionable subsidies

Actionable subsidies—that is, subsidies that are not prohibited—may cause adverse effects/serious prejudice to the economic interests of other WTO Members, contrary to Articles 5 and 6 of the ASCM. These prejudicial effects include market phenomena such as “lost sales,” “displaced

or impeded imports,” “significant price suppression,” or “significant price undercutting.” If subsidies have such effects on other WTO Members, they are, strictly speaking, not prohibited, but must nevertheless be withdrawn or their effects must be removed (Article 7.8, ASCM).

A challenge to such subsidies is potentially complex and requires extensive economic evidence. So far, five sets of disputes have featured claims under Article 6.3 of the ASCM, resulting in very lengthy and complex awards in three of these sets of disputes.⁴¹

What is of interest for our purposes is the legal standards interpreted and applied by WTO adjudicative bodies for demonstrating serious prejudice. Less exacting standards of proof may encourage more challenges, limiting policy space for subsidizing members; conversely, stricter standards would have the opposite effects, deterring further potential complainants. For instance, panels and the Appellate Body have had to determine how to assess, methodologically, whether particular price effects or other effects (such as lost sales or displaced imports in third markets) are attributable to a subsidy. They have also had to decide other methodological questions such as whether a subsidy must be quantified; whether a pass-through analysis may be required; or under which conditions different subsidies may be considered cumulatively when analyzing their impact on the market.

The case law on serious prejudice has been criticized by some commentators and practitioners as being confusing, uncertain, and unpredictable; in contrast, others have criticized it as being too lenient on the standard of proof to be adduced by the complainant (Sapir and Trachtman 2008). For instance, some have criticized that the complainant need not quantify the amount of the subsidy and, more generally, that the overall economic analysis is not sufficiently rigorous.⁴² Regardless of the merit of these views, the approach of WTO panels and the Appellate Body will have an impact on the willingness of Members to bring adverse effects/serious prejudice challenges. Lesser willingness to

39 Export duties are permitted under WTO law, except for some WTO Members that have acceded after 1995 and have taken on certain additional commitments in their Protocol of Accession, such as China, Russia, and Vietnam. Panel Report, *US – Export Restraints*, para. 8.75.

40 This has been used, for instance, by Argentina and Indonesia to foster biodiesel industries that use locally produced soy bean oil or palm oil as input. However, as previously noted, the EU has a practice of using surrogate prices in such circumstances when conducting anti-dumping investigations and calculating cost benchmarks or constructed normal value. See the earlier example concerning trade remedy measures.

41 *Indonesia – Autos* (DS54/DS55/DS59/DS64); *Korea – Commercial Vessels* (DS273); *US – Upland Cotton* (DS267); *EC and certain member States – Large Civil Aircraft* (DS316); *US – Large Civil Aircraft* (2nd complaint) (DS353).

42 Panel report, *US – Upland Cotton*, paras. 7.1297 and 7.1300; and the Appellate Body Report, *US – Upland Cotton*, para. 473. For a critique of these findings, see Sapir and Trachtman (2008), pp. 194, 197.

bring such challenges signifies greater effective policy space for subsidizing Members.

Another interesting aspect are serious prejudice/adverse effect challenges against subsidies granted by developing countries. Articles 27.8 and 27.9 of the ASCM appear to limit the scope of multilateral challenges brought against actionable subsidies granted by developing countries. More specifically, it appears that developing countries may not be subject to serious prejudice claims pursuant to Articles 5(c) and 6.3. Rather, only claims relating to injury (under Article 5(a)) and nullification and impairment (Article 5(b)) may be brought, relating to the subsidizing Member's and to the complaining Member's market. This means that serious prejudice in the subsidizing Member's market and in third markets could not be the basis for a challenge. However, at least some academic commentators question this view and argue that serious prejudice claims against developing countries' subsidies remain possible.⁴³ A clarification of Article 27.9 by a panel would thus help define the policy scope for developing countries on actionable subsidies by defining the challengeability of such subsidies in the WTO. This would be of use only to those developing countries that can afford to provide subsidies.

Product Standards under the TBT and SPS Agreements

As previously noted, an area of domestic regulation with ever-increasing importance is product standards. Here, I use the term "product standards" rather loosely to designate any governmental rule that lays down product requirements. These requirements may determine either whether a product may be marketed at all or may use particular product-related conditions to determine eligibility for certain treatment, for example, the right to bear certain labels. The legal disciplines applicable to product requirements include the GATT 1994 as well as, most prominently, the TBT and SPS Agreements. The SPS Agreement is essentially a *lex specialis* to the TBT Agreement, enshrining a special regime for product standards for food and animal feed as well as for measures intended to prevent the spread of pests and diseases. Unusually for WTO law, TBT Agreement disciplines include not only mandatory technical specifications, but also non-binding technical "standards" promulgated by standardizing bodies. Moreover, a lively policy and legal debate has been raging about the appropriate legal treatment of so-called private standards, that is, product requirements imposed and operated by private market actors with significant market power, such as, for example, supermarkets or other large retailers. Finally, special attention has also been devoted to product standards that relate to the methods by which products are produced, as opposed to the physical characteristics of the resulting products.⁴⁴

As noted above, product standards can result in significant market entry barriers. First, market entry barriers will arise simply because different standards exist in different markets—which increases production costs. Another, and more complicated, layer of problems arises when product

standards are so demanding (restrictive) as to render compliance physically or at least commercially impossible for certain suppliers (for instance, those in developing countries). There are different ways of thinking about industrial policy and product standards. If we define industrial policy as a deliberate, targeted, and sustained policy to foster domestic industries to enhance their competitiveness, provide greater value added, or better integrate them into global value chains, then WTO-consistent technical regulations and standards are not a tool that a government would want to use. WTO disciplines are designed to ensure that product standards do not skew competitive conditions and impose unnecessary barriers to trade. WTO disciplines also encourage international harmonization, in pursuit of an (ideal) trading environment in which different markets accept each other's standards as equivalent or, even better, follow similar or identical standards previously elaborated by international standardizing bodies. An attempt by a WTO Member to enhance the competitive opportunities of a domestic industry through product standards that, for whatever reason, will benefit or will be complied with more easily by the domestic industry is likely to be struck down by the WTO dispute settlement system.

By way of example, such measures may contravene Article 2.1 (discrimination) or 2.2 (unnecessary trade barriers) of the TBT Agreement or Article 5.6 of the SPS Agreement (unnecessary trade barriers). Where a measure pursues both a legitimate goal—for instance, product safety or consumer information—but is also discriminatory or otherwise skews the competitive field, that measure will be struck down either in its entirety or at least partially, assuming it is possible to isolate the legitimate aspects of the measure from its discriminatory aspects.

As previously noted, it is of course possible that exacting, but non-discriminatory product standards will indirectly prove to be beneficial for the domestic industry. For instance, it is possible that particular labeling standards or environmentally motivated requirements may strengthen consumer demand for locally produced products. Similarly, very strict hygiene requirements could result in limiting the range of enterprises capable of supplying products of the required quality; these requirements may thereby in practice shut out certain supplier countries from the regulating Member's market. If we include such indirect effects in the concept of "industrial policy," then the picture changes—WTO case law can enhance policy space by interpreting provisions of the TBT and SPS Agreements in a manner advantageous to the regulating Members.

43 For a detailed summary of the relevant views, see Coppens (2014), from pp. 268.

44 A particularly hotly debated question relates to processes and production methods that do not give rise to particular physical features of the resulting product.

For instance, WTO adjudicatory bodies will in the future have the opportunity to define with greater precision the level of scientific evidence that Members will require as a sufficient basis for domestic regulation. This will be particularly relevant for measures whose effects may allegedly materialize only at a later point in time. Findings on this issue will determine, for instance, the reach of Article 2.2 of the TBT Agreement, which requires that technical regulations not be more trade restrictive than necessary to achieve a particular objective. Similarly, the approach to identifying less trade-restrictive regulatory alternatives will be crucial to the practical reach of the disciplines under Article 2.2.

By way of another example, the requirement under Article 5.5 of the SPS Agreement requiring consistency in the level of protection across comparable situations (that is, how risk-averse or how risk-friendly regulation is across a range of comparable contexts) could be interpreted more strictly or more leniently in future disputes. If regulating Members may adopt more divergent levels of protection (risk attitudes) in different regulatory contexts, they will have more policy space to regulate particular economic sectors more strictly or leniently.

There are many other provisions under the TBT and SPS Agreements whose interpretation and application will make the adoption of product requirements easier or more difficult. All of these decisions will affect the policy space for WTO members in promulgating product standards.

Government procurement

Governments often pursue industrial policy through government procurement practices. Government procurement is in principle excluded from the strictures of the GATT 1994 as well as from the GATS. However, certain WTO Members have signed up to the Government Procurement Agreement (GPA), which limits their discretion with respect to procurement by the listed entities and agencies.⁴⁵ For areas of government procurement outside GPA commitments, Article III:8(a) of the GATT 1994 is crucial because it exempts measures "governing the procurement by governmental agencies of products purchased for governmental purposes" from the strictures of Article III, especially the national treatment requirement under Article III:2 and III:4. In other words, in those areas, governments may pursue industrial policy, for instance, by providing preference to domestic goods over imported goods.

The dispute in *Canada – Feed-in Tariff Program* demonstrated that Article III:8(a) could be read narrowly or broadly. The question that arose was whether the protective effect of the phrase "governing the procurement ... of products" was triggered when the discrimination concerned products that were not the same as the product being procured. In the dispute, the government was (according to Canada) procuring electricity from renewable electricity suppliers. However, the discrimination challenged by the complainants concerned the energy generation equipment, such as wind

turbines. As noted earlier, the government required that the electricity purchased by it had to be generated, for instance, with domestic wind turbines. The panel found that there was sufficient proximity between these two sets of products (electricity and wind turbines) to trigger Article III:8 and, subject to compliance with the remaining conditions,⁴⁶ would shield the measure from the remainder of the Article III disciplines. In contrast, the Appellate Body ruled that, in order to trigger Article III:8, the product to be granted exemption from Article III, including the national treatment requirement, must be in a "competitive relationship" with the foreign product "allegedly being discriminated against."⁴⁷ This was clearly not the case for electricity and the generation equipment.⁴⁸

Thus, the panel's interpretation would have provided a potentially wide margin of discretion for governments to conduct industrial policy by discriminating in favour of a domestic product as long as that product was sufficiently closely related to the product being procured. Arguably, this would have greatly expanded the product spectrum exempt from Article III and the national treatment principle. In contrast, the Appellate Body reduced the eligible product scope and thus also reduced the policy space available. Equal treatment may be denied only to the product actually procured, not also to a product vaguely related to the procured product or to machinery that produces the procured product.

However, the Appellate Body explicitly left open whether the exemption clause of Article III:8(a) applied to goods incorporated into the product procured,⁴⁹ that is, whether for instance a government that procures cars for governmental use may permissibly require that only cars with domestic tires and engines will be eligible for procurement. This is an important question, the answer to which may result

⁴⁵ The current GPA parties are Armenia, Canada, EU-28, Hong Kong, China, Iceland, Israel, Japan, Korea, Liechtenstein, Netherlands with respect to Aruba, Norway, Singapore, Switzerland, Chinese Taipei, and the US.

⁴⁶ Given that only electricity generated with locally sources equipment was eligible for governmental purchase under the FIT programme, the Panel was of the view that the fulfillment of the local content requirements was "a necessary prerequisite" for the procurement to take place and therefore the "requirement 'govern' the alleged procurement" (Panel Report, *Canada – Feed-in Tariff Program*, paras. 7.124, 7.126, 7.127). However, the panel ultimately ruled that Article III:8(a) did not apply because the government was not acquiring the electricity for governmental use, but rather for resale (para. 7.151).

⁴⁷ Appellate Body Report, *Canada – Feed-in Tariff Program*, paras. 5.63, 5.79.

⁴⁸ In any event, Canada was found not to have procured electricity for governmental use, but rather to have bought and resold that electricity.

⁴⁹ The Appellate Body found that "[w]hat constitutes a competitive relationship between products may require consideration of inputs and processes of production used to produce the product," but declined to decide whether the "derogation in Article III:8(a)" extends to such forms of discrimination (Appellate Body Report, *Canada – Feed-in Tariff Program*, para. 5.63).

in broader or narrower policy space for governments to support domestic industries via government procurement. However, the significance of this question will also wane as the membership and coverage of the GPA expands, because its non-discrimination clause will render the interpretation of Article III:8(a) moot.⁵⁰

State trading enterprises

State trading enterprises are regulated in Article XVII of the GATT 1994. In *Canada – Wheat*, the Appellate Body issued an important ruling under this provision, finding that the requirement that state trading enterprises must act “solely in accordance with commercial considerations” under Article XVIII:1(b) did not constitute a separate requirement from the requirement that these enterprises “act in a manner consistent with the general principles of non-discriminatory treatment,” as required in Article XVII:1(a).⁵¹ This finding left state trading enterprises—and the regulating WTO Members—with more policy space, because state trading enterprises often conduct their operations not only from a commercial perspective, but also may pursue other goals, for instance, price or sustainability policies. This ruling may be particularly important for WTO Members where numerous state trading enterprises and state-owned enterprises with special privileges operate.

However, *Canada – Wheat* left open whether the term “general principles of non-discriminatory treatment” includes only the most-favored nation principle, or also national treatment. Arguably, a requirement to observe the national treatment requirement, in addition to the most-favored nation requirement, may at least in some circumstances interfere with the functioning of at least some state trading enterprises, for instance, marketing boards that purchase from local producers at particular prices. Should WTO panels and the Appellate Body be called upon to clarify the scope of Article XVII:1(a) and should they explicitly rule that this provision does not imply a national treatment requirement, this would result in, or confirm, greater policy space for WTO Members operating such enterprises.

CONCLUSION

The paper has considered a number of examples of how existing or potential interpretations and findings of WTO adjudicatory bodies may impact on the policy space of WTO Members to implement industrial policy measures.

The many examples listed above demonstrate that WTO dispute settlement can, at the margin and in some instances, affect the policy space available for Members to pursue industrial policy objectives. The dispute settlement bodies may also, through their interpretation and application of the law, influence the willingness of potential claimants to bring challenges before the WTO. However, it bears repeating that the ability of dispute settlement decisions to impact WTO Members' policy space for industrial policy is strictly circumscribed by the existing treaty rules that WTO panels and the Appellate Body have to take as a given.

⁵⁰ Nevertheless, it may be noted that developing countries may negotiate exceptions from the national treatment obligation, pursuant to Article V:4 of the GPA.

⁵¹ Appellate Body Report, *Canada – Wheat*, para. 100.

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