United States – Tax Treatment for “Foreign Sales Corporations”: Second Recourse to Article 21.5 of the DSU by the European Communities

(AB-2005-9)

APPELLEE SUBMISSION OF THE UNITED STATES OF AMERICA

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United States – Tax Treatment for “Foreign Sales Corporations”: Second Recourse to Article 21.5 of the DSU by the European Communities

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SERVICE LIST

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I. Introduction and Executive Summary

1. In its Notification of an Other Appeal, the European Communities ("EC") has made several contingent claims of error, all of which the Appellate Body should reject.\(^1\)

2. First, with respect to the EC’s claims that the United States has failed to comply with its obligations under Article 4.7 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") and Articles 19.1 and 21.1 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), the EC’s claims fail because none of these provisions imposes obligations on WTO Members.

3. Second, with respect to the EC’s request that the Appellate Body make recommendations under Article 4.7 of the SCM Agreement or Article 19.1 of the DSU, there is no claim before the Appellate Body that either the first Article 21.5 Panel or the second Article 21.5 Panel erred by not making recommendations under either provision. Therefore, the contingency that would trigger the EC’s request – a finding that either or both panels erred by not making recommendations – simply does not and will not exist.

4. Third, the EC failed to comply with the requirements of Articles 23(3) and 21(2) of the Working Procedures for Appellate Review ("Working Procedures").

5. Finally, with respect to the EC’s “claims” of error under Articles 3 and 11 of the DSU, the EC also failed to address these claims in its Other Appellant Submission, as it was required to do by Articles 23(3) and 21(2) of the Working Procedures. Therefore, the Appellate Body should dismiss these “claims.”

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\(^1\) WT/DS108/33 (30 November 2005). The United States notes at the outset that this appellee submission addresses only the contingent claims of error alleged by the EC in its Notification of an Other Appeal. This submission does not address the many other inaccuracies in the Other Appellant’s Submission by the European Communities, 29 November 2005 ("EC Other Appellant Submission").
II. Articles 19.1 and 21.1 of the DSU Do Not Impose Obligations on Members

6. With respect to the EC’s claims that the United States has failed to comply with its obligations under Articles 19.1 and 21.1 of the DSU, the Appellate Body should reject the EC’s claims for the simple reason that neither provision imposes obligations on WTO Members.

7. Article 19.1 provides as follows:

Where a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring the measure into conformity with that agreement. In addition to its recommendations, the panel or Appellate Body may suggest ways in which the Member concerned could implement the recommendations. (Footnotes omitted).

The first sentence of Article 19.1 does impose an obligation (“shall recommend”), but imposes it on panels and the Appellate Body. The second sentence of Article 19.1 does not even impose an obligation, but instead confers on panels and the Appellate Body the discretionary authority to make suggestions as to how the Member concerned could implement recommendations.

8. Notwithstanding the clear language of Article 19.1, the EC asserts that Article 19.1 imposes an “implicit obligation” on Members. However, to take a directive aimed at panels and the Appellate Body and interpret it so as to impose an obligation on Members would be an exercise in law-making under the guise of interpretation. This type of covert legislation is precisely what is prohibited by Article 19.2 of the DSU, which provides that “in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements.”

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2 WT/DS108/33 (30 November 2005), para. 2(b).
3 EC Other Appellant Submission, para. 17.
9. Turning to Article 21.1 of the DSU, it provides as follows: “Prompt compliance with recommendations or rulings of the DSB is essential in order to ensure effective resolution of disputes to the benefit of all Members.” Article 21.1 is not directed at anyone in particular, and does not even impose an obligation. Instead, it articulates a goal of the dispute settlement system. As such, it is similar to Article III:1 of the General Agreement on Tariffs and Trade 1994, which the Appellate Body has found contains general principles that inform the specific obligations found in Article III. To read into Article 21.1 an implicit obligation on Members, as suggested by the EC, would run afoul of Article 19.2 of the DSU for the same reasons discussed above in connection with the EC’s attempt to rewrite Article 19.1.

10. The position that Articles 19.1 and 21.1 of the DSU do not impose obligations on Members is straightforward and unremarkable. It is based on what the text actually says. It also is the position taken before the Panel by Brazil and Australia, the two third parties that chose to respond to a question from the Panel on this issue.

4 Japan – Alcohol (AB), pages 17-18.

With respect to Brazil, it stated as follows:

Brazil considers that a WTO Member cannot violate Articles 19.1 and 21.1 of the DSU. Article 19.1 sets out an obligation on panels and the Appellate Body to recommend that a Member found in breach of its multilateral commitments bring the illegal measure into conformity with the covered agreements. Article 21.1, in turn, expresses a fundamental objective and basic principle of the WTO dispute settlement system.

Responses by Brazil to Questions posed by the Panel, 11 July 2005, Question 10, page 3 (italics in original).

As for Australia, it stated as follows:

Article 19.1 of the DSU does not give rise to independent and enforceable
11. The EC confuses the important role that recommendations play with an obligation on Members. The recommendations, when adopted by the DSB, are the official multilateral recommendation that a Member bring an inconsistent measure into conformity. The recommendation, as the first sentence of Article 19.1 makes clear, is premised on an official finding that the measure is inconsistent with a covered agreement, and certain consequences flow from a recommendation. As noted by Australia in its response to the Panel’s questions, a Member that fails to implement an adopted recommendation under Article 19.1 may have to offer compensation or face suspension of concessions. However, any inconsistency is an inconsistency with the relevant provision of the covered agreements; it is not an inconsistency with Article 19.1 or 21.1. The recommendation does not itself give rise to a new and separate obligation. Indeed, Article 19.2 explicitly states that recommendations cannot “add to” the obligations provided in the covered agreements.

12. In this regard, the Appellate Body’s characterization of Article 17.6(i) of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 is obligations on the parties to the dispute. It is the recommendation of a panel and/or the Appellate Body (as adopted by the DSB) mentioned in the first sentence of Article 19.1 that gives rise to independent and enforceable obligations on the parties to the dispute (in the sense that a WTO Member that fails to comply with the recommendation may find itself liable to provide compensation or face the suspension of concessions or other obligations).

Article 21.1 of the DSU outlines the fundamental importance of prompt compliance with the recommendations and rulings of the DSB. It provides important context for the interpretation of the remainder of Article 21 of the DSU and of Article 22 of the DSU, which set out the possible consequences of failing to promptly comply with the recommendations and rulings of the DSB.

Australia response to the questions from the Panel, 11 July 2005, Question 10, pages 1-2.
informative. Article 17.6(i) sets forth the standard of review to be applied by a panel in its assessment of the facts in a dispute involving an anti-dumping measure. The Appellate Body has found that Article 17.6(i) effectively “defines when investigating authorities can be considered to have acted inconsistently with the Anti-Dumping Agreement in the course of their ‘establishment’ and ‘evaluation’ of the relevant facts.” In other words, Article 17.6(i) has practical consequences for investigating authorities. At the same time, however, the Appellate Body has recognized that Article 17.6(i) does not impose an obligation on Members.

13. Accordingly, for the foregoing reasons, the Appellate Body should reject the EC claim that the United States has failed to comply with its alleged obligations under Articles 19.1 and 21.1 of the DSU.

III. Article 4.7 of the SCM Agreement Does Not Impose Obligations on Members

14. With respect to the EC’s claim that the United States has failed to comply with its obligations under Article 4.7 of the SCM Agreement, the Appellate Body should reject the EC’s claim because that provision, like Articles 19.1 and 21.1 of the DSU, does not impose obligations on WTO Members.

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6 US – Hot-Rolled Steel (AB), para. 56 (italics in original).
7 Thailand – H-Beams (AB), para. 114 (“Articles 17.5 and 17.6 . . . do not place obligations on WTO Members”); see also US – Hot-Rolled Steel (AB), para. 56 (“[T]he text of Article 17.6(i) is couched in terms of an obligation on panels ...”) (italics in original).
8 WT/DS108/33 (30 November 2005), para. 2(a).
9 The United States disagrees with the EC assertion that the Panel “did not rule” on the EC’s Article 4.7 claims. EC Other Appellant Submission, Section II (heading). As explained in the Appellant Submission of the United States of America, November 21, 2005, paras. 17-44 (“U.S. Appellant Submission”), the Panel clearly made findings under Article 4.7, albeit findings that were in error.
15. Article 4.7 is a special or additional rule or procedure within the meaning of Article 1.2 of the DSU. Its function in prohibited subsidies disputes is similar to the function of Article 19.1 of the DSU in general WTO disputes.\textsuperscript{10} Article 4.7 provides as follows:

If the measure in question is found to be a prohibited subsidy, the panel shall recommend that the subsidizing Member withdraw the subsidy without delay. In this regard, the panel shall specify in its recommendation the time period within which the measure must be withdrawn.

Like Article 19.1, Article 4.7 is addressed to panels, not Members. Article 4.7 obligates panels, in certain circumstances, to make a withdrawal recommendation and specify the time period for withdrawal. Thus, a Member cannot be said to “violate” Article 4.7.

16. As it does with respect to Article 19.1 and 21.1 of the DSU, the EC argues that notwithstanding the text, Article 4.7 of the SCM Agreement contains an implicit obligation on Members. Again, however, to take a directive aimed at panels and interpret it so as to impose an obligation on Members would be inconsistent with Article 19.2 of the DSU.

17. Indeed, it is telling that the EC’s argument is not based on the text of Article 4.7, but instead is based on the EC’s interpretation of statements made by the Appellate Body in its report in \textit{US – FSC (Article 21.5) (AB)}. Specifically, the EC cites to paragraph 229 of the report, in which the Appellate Body states that Article 4.7 “requires prohibited subsidies to be withdrawn”.\textsuperscript{11} In addition, the EC cites to paragraph 230 of the report, in which the Appellate Body states that Article 4.7 “requires prohibited subsidies to be withdrawn”.

\textsuperscript{10} The EC appears to share this view. \textit{See} EC Other Appellant Submission, para. 19.

\textsuperscript{11} EC Other Appellant Submission, para. 12, \textit{quoting US – FSC (Article 21.5) (AB)}, para. 229.
Body refers to “a Member’s obligation under Article 4.7 of the SCM Agreement to withdraw prohibited subsidies ... .”\(^{12}\)

18. In the view of the United States, this is an insufficient basis for a claim that Article 4.7 imposes an obligation on Members. First, it assumes that the Appellate Body ignored the clear text of Article 4.7 and acted inconsistently with its own obligation under Article 19.2 of the DSU to refrain from “add[ing] to or diminish[ing] the rights and obligations provided in the covered agreements.”

19. Second, the passages quoted by the EC are consistent with the proposition that Article 4.7 (together with Article 4.10) defines the consequences of a finding that a measure is a prohibited subsidy – if it is not withdrawn within the specified time period, the DSB “shall grant” authorization to the complaining Member to take appropriate countermeasures. But it is Article 3.2 of the SCM Agreement, not Article 4.7, that prohibits the granting or maintenance of prohibited subsidies. The EC’s approach would have troubling consequences, such as in situations in which a finding is made under Article 3 of the SCM Agreement that a measure is a prohibited subsidy, but the provisions of Article 30 rather than Article 4 have been invoked (for example, because there are other claims not involving prohibited subsidies). The United States wonders if the EC means to argue that in that instance there would be no obligation to withdraw the subsidy.

20. Finally, it is significant that in \textit{US – FSC (Article 21.5)}, neither the panel nor the Appellate Body found a violation of Article 4.7 of the SCM Agreement. Instead, the panel

merely found that the United States had “failed to implement the recommendations and rulings of the DSB made pursuant to Article 4.7 of the SCM Agreement”,\(^{13}\) while the Appellate Body merely upheld the panel’s finding.\(^{14}\) Thus, the issue of a supposed U.S. “violation” of Article 4.7 was not even before the Appellate Body.

21. Thus, for the foregoing reasons, the Appellate Body should reject the EC’s conditional claim that the United States failed to comply with its obligations under Article 4.7 of the SCM Agreement.

**IV. The Appellate Body Should Reject the EC’s Contingent Request for Recommendations Under Article 4.7 of the SCM Agreement or Article 19.1 of the DSU**

22. The EC requests that if the Appellate Body should find that the Panel erred in concluding that no new recommendations were necessary under Article 4.7 of the SCM Agreement or Article 19.1 of the DSU, then the Appellate Body should issue the necessary recommendations.\(^{15}\) The Appellate Body should reject the EC’s request, because it is impossible that the contingency triggering the EC’s request could arise. The U.S. Notice of Appeal did not include a claim that the Panel erred in concluding that no new recommendations were necessary.\(^{16}\) The EC Notice of

\(^{13}\) *US – FSC (Article 21.5) (Panel)*, para. 9.1(e).
\(^{14}\) *US – FSC (Article 21.5) (AB)*, para. 256(f).
\(^{15}\) WT/DS108/33 (30 November 2005), para. 3.
\(^{16}\) See WT/DS108/32 (16 November 2005). Indeed, the United States alleged that the Panel erred by even suggesting that it had the authority to make new recommendations. See *id.*, para. 1, in which the United States claimed that the Panel erred by concluding that “a panel established under Article 21.5 of the DSU may make a recommendation pursuant to Article 4.7 of the SCM Agreement.” However, in its appellant submission, the United States explained that given the systemic nature of this issue, it did not believe it best to pursue this particular claim of error in this limited appeal. U.S. Appellant Submission, note 36.
Other Appeal did not contain such a claim either. Therefore, there would be no basis for the Appellate Body to find that the Panel erred by not making new recommendations.\footnote{See, e.g., \textit{US – Cotton Subsidies (AB)}, paras. 494-495; and \textit{EC – Bananas III (AB)}, para. 152.}

23. Moreover, the EC never addresses the fact that Article 4.7 refers to the “panel” and contains no reference or express grant of authority to the Appellate Body. Nor has the EC addressed the consequences of a recommendation under Article 4.7. The Panel expressly found that “Similarly, in a dispute involving a subsidy already found to be prohibited, if an Article 21.5 panel made a recommendation under the first sentence of Article 4.7 of the SCM Agreement to withdraw the prohibited subsidy ‘without delay’, the panel would also presumably be required to ‘specify … the time-period within which the measure must be withdrawn. This would, in effect, amount to giving an additional period of time for the Member concerned to withdraw the prohibited subsidies.”\footnote{Panel Report, para. 7.44.} The EC has not appealed this panel finding, and it would be adopted together with any new recommendation under Article 4.7 that the EC seeks.

24. Thus, for the foregoing reasons, the Appellate Body would not be in a position to grant the EC’s request, even if the contingency upon which that request depends were to occur. Therefore, the Appellate Body should reject the EC’s request.

\footnote{The United States notes that the EC’s contingent request encompasses the report of the panel in the first Article 21.5 proceeding. EC Other Appellant Submission, para. 27. That panel report is not a subject of the U.S. appeal, and the EC fails to explain how a report adopted by the DSB in 2002 could be the subject of an appeal in 2005, or under what authority the Appellate Body could “complete the panel’s analysis” with respect to a panel report that already has been adopted.}
V. The EC Claims Also Fail Due to the EC’s Failure to Comply with Rule 21 of the Appellate Body Working Procedures

25. There is an additional ground for dismissing the EC’s claims. The EC has failed to file a submission that complies with the requirements of Rule 21(2)\(^\text{19}\) of the *Working Procedures*. Rule 21(2)(b) provides, in relevant part, that the written submission of an appellant:

    shall ... set out

    (i) a precise statement of the grounds for the appeal, including the specific allegations of error in the issues of law covered in the panel report and legal interpretations developed by the panel, and the legal arguments in support therefor; [and]

    (ii) a precise statement of the provisions of the covered agreement and other legal sources relied on [.]

26. The EC Other Appellant Submission does not, however, set out the required “precise statements.” Instead, as the EC itself says: “In Section II below, the European Communities will briefly summarise for the convenience of the Appellate Body the first two claims [*i.e.*, the claims in question], the remaining undecided elements of which it submits again to the Appellate Body. The detailed arguments supporting these claims can be found in the EC submissions before the Panel and are hereby incorporated by reference.”\(^\text{20}\)

\(^{19}\) Rule 21(2) applies in this situation pursuant to Rule 23(3) of the *Working Procedures*.  
\(^{20}\) EC Other Appellant Submission, para. 6. Furthermore, while Section II(A) relies on “the reasons set out in more detail in [the EC’s] submissions to the Panel” (EC Other Appellant Submission, para. 15), and section II(B) relies on the “reasons ... set out in [the EC’s] submissions to the Panel” (EC Other Appellant Submission, para. 22), in neither case does the EC actually state those reasons. In footnotes, the EC does direct the reader to particular paragraphs of its submissions, but the EC does not even purport to give an exhaustive list: the lists of paragraphs begin with an “*e.g.* [*exempli gratia*, in other words ‘for example’].”
27. While it may perhaps be possible to comply with Rule 21 through an incorporation by
reference, the EC certainly has not complied in this instance, for the following reasons.

28. First, the EC’s vague references do not meet the Rule’s standard of setting arguments
out, let alone providing a precise statement of the legal arguments and of the provisions relied
on. Leaving the Appellate Body (and the United States and the third participants) to guess which
arguments in which separate documents are relevant is the exact opposite of providing a “precise
statement” of those arguments in the other appellant submission. For example, in Section II(A)
of its submission the EC addresses an alleged violation of Article 4.7 of the SCM Agreement,
referring the reader – in footnote 6 – to the EC’s response to the Panel’s question 10. But that
question is about Articles 19 and 21 of the DSU.

29. Second, the EC’s approach ignores the interests reflected in Rule 21 of the third
participants. The EC has referred in its footnotes to submissions (in particular, its oral
statements and its responses to the Panel’s questions) that were never served on the third parties.
The opening statement of the EC was reprinted as an annex to the Panel Report, but the EC’s
closing statement and its responses to questions were not. Nor are these materials posted on
the EC’s website.

30. Accordingly, Section II of the EC Other Appellant Submission fails to comply with
Rule 21 of the Working Procedures. Pursuant to Rule 29, the Division may dismiss that portion

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21 For example, where the submissions being incorporated are available to all the
participants and third participants and clearly identify and express the precise arguments in a
coherent, discrete manner.

22 In this connection, we note that in footnote 6 of the EC Submission the EC also refers
to its closing statement at the meeting of the Panel. The United States has no record of the EC
submitting a written version of its closing statement to the Panel.
of the EC’s appeal to which Section II relates if it considers that such an order would be appropriate. The EC’s failure to abide by the Appellate Body *Working Procedures* is another reason to reject the EC’s claims.

**VI. The Appellate Body Should Dismiss the EC’s “Claims” Concerning Articles 3 and 11 of the DSU**

31. In its Notice of Other Appeal, the EC states:

   [I]f the Appellate Body were to find that the Panel had erred, this would mean that the Panel had not conducted its assessment of the matter in accordance with Article 11 of the DSU and had not contributed to an effective resolution of the dispute within the meaning of Article 3 of the DSU.23

   It is unclear whether this curiously worded statement actually asserts contingent claims of error involving Articles 3 and 11 of the DSU.

32. However, even if the Appellate Body were to consider that the statement does advance claims of error, the Appellate Body should dismiss these “claims.” Insofar as these “claims” are concerned, even assuming for purposes of argument that the EC Notice of Other Appeal satisfied the requirements of Article 23(2) of the *Working Procedures*, the EC Other Appellant Submission failed to satisfy the requirements of Article 21(2) and 23(3) of the *Working Procedures*. With respect to an Other Appeal, Article 23(3) requires the filing of “a written submission prepared in accordance with paragraph 2 of Rule 21 . . . .” Rule 21(2), in turn, provides, in relevant part, that the written submission:

   shall ... set out

   (i) a precise statement of the grounds for the appeal, including the specific allegations of error in the

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23 WT/DS108/33 (30 November 2005), para. 4.
issues of law covered in the panel report and legal interpretations developed by the panel, and the legal arguments in support thereof;

(ii) a precise statement of the provisions of the covered agreement and other legal sources relied on; and

(iii) the nature of the decision or ruling sought.

33. With respect to the EC’s “claims” concerning Articles 3 and 11 of the DSU, the EC Other Appellant Submission does not contain a precise statement of the grounds for the appeal, does not contain a precise statement of the provisions of the covered agreement and other legal sources relied on, and does not indicate the nature of the decision or ruling sought. Indeed, the EC Other Appellant Submission does not mention Articles 3 or 11 of the DSU at all.

34. Due to the EC’s failure to comply with Articles 23(3) and 21(2) of the Working Procedures, the United States has been denied an opportunity to contest the EC’s “claims” because it does not even know what the EC’s arguments are.\(^\text{24}\) Under these circumstances, the EC’s “claims” should be dismissed.

VII. Conclusion

35. For the reasons set forth above, the United States respectfully requests that the Appellate Body reject the contingent claims of error advanced by the EC.

\(^{24}\) It is also possible that the EC decided not to pursue its claims regarding Articles 3 and 11.