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## **CHINA'S 'GOING GLOBAL' POLICY: TRANSNATIONAL SUBSIDIES UNDER THE WTO SCM AGREEMENT**

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## Abstract

As China is increasingly 'going global', foreign direct investment under its Belt and Road Initiative is coming under scrutiny. One of the concerns is that Chinese companies establishing themselves in third countries would be unfairly advantaged by the financing they receive under China's expansionist strategy. This financing gives rise to a situation, which had long been described as 'unrealistic', in which a government subsidizes a firm outside of its territory. Could such financing, which has a transnational element, be disciplined under the WTO Agreement on Subsidies and Countervailing Measures? Should such financing, which enhances development in the receiving countries, be disciplined at all? The authors shed light on these issues and provide preliminary guidance on how to structure the problem under international trade law.

## Keywords

Transnational Subsidies, World Trade Organization, Belt and Road Initiative, Foreign Direct Investment.

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## Introduction

Due to the heavy involvement of the Chinese government throughout its economy, the issue of Chinese subsidies has recently gained considerable attention. The trilateral group of the United States of America (**US**), the European Union (**EU**), and Japan on this issue is evidence of a new political momentum to strengthen discipline on Chinese subsidies, particularly considering China's growing importance to the global economy. So far, the spotlight has been mainly on how to define the 'givers' of the subsidies in China,<sup>1</sup> with only little attention given to the situation of the recipients.

In his recent book, Professor Marc Benitah defines a transnational subsidy as 'a subsidy granted to a benefit recipient manufacturing the product at issue outside the country of the granting government'.<sup>2</sup> In a footnote to this definition, he explains that a definition that allows for the inclusion of a situation in which 'a government subsidizes a firm which is not under its jurisdiction' should not be considered as it is 'unrealistic'.<sup>3</sup>

As China increasingly 'goes global' through its Belt and Road Initiative (**BRI**), it funds projects in third countries and assists Chinese-owned companies in establishing themselves abroad. As a result, the European Commission (**Commission**) is currently faced with this 'unrealistic' scenario in three anti-subsidy investigations.

This article aims to assess whether transnational subsidies, i.e., the government subsidization of a firm outside of its territory, can be disciplined under the Subsidies and Countervailing Measures (**SCM**) Agreement. As transnational subsidies are now culminating under the BRI, this article will take financing under the BRI as example in its analysis. The BRI being perceived as catalysing development and distorting trade simultaneously, this article will attempt to balance this contradiction.

It will first provide a historical background describing the emergence of transnational subsidies in the context of China's outward expansion [Section 2]. Then, this article will move on to analyse whether transnational subsidies fall within the ambit of the SCM Agreement [Section 3]. Section 4 elaborates on whether transnational subsidies should be disciplined from a policy perspective. A comparison of how Members of the World Trade Organization (**WTO**) have addressed transnational subsidies in their national laws is provided next [Section 5]. Section 6 concludes this article.

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<sup>1</sup> See *generally*, Chad Bown & Jennifer Hillman, *WTO'ing a Resolution to the China Subsidy Problem*, 23(4) JOURNAL OF INTERNATIONAL ECONOMIC LAW (2019).

<sup>2</sup> Marc Benitah, *THE WTO LAW OF SUBSIDIES, A COMPREHENSIVE APPROACH* 605 (Wolters Kluwer, 2019) [hereinafter 'Benitah, SUBSIDIES'].

<sup>3</sup> *Id.*

## 1. The Emergence and Increasing Relevance of Transnational Subsidies

Before the Second World War, subsidies were perceived only as a tool for countries to spur industrialization and create economic growth in desired sectors at home. Since then, globalization has increased in an unabated manner. Subsidies have thus taken on international elements. This has now culminated in China's 'going out' policy, whereby the Government of China uses various types of financial assistance to help Chinese companies to establish themselves in third countries.

### 1.1. From National Subsidies to Transnational Subsidies

After the end of the Second World War, governments realized that subsidies could have potential trade distorting effects.<sup>4</sup> As a result, countries discussed imposing some form of discipline on them in the Havana Charter, which should have given birth to the International Trade Organization, and in the GATT 1947. However, the GATT 1947 ended up being rather lenient towards subsidies, which kept the door open for countries to compete in subsidizing their exporters in order to defend their national interests in the global market as well as create economic growth at home.<sup>5</sup>

By the 1970s, the use of subsidies had become one of the most frequently used and controversial commercial policies.<sup>6</sup> During the economic slowdown in the 1970s, countries responded by extending their subsidy programs to their domestic industries in order to boost their economy and protect employment leading to, what the GATT Director General called, trade based on 'competitive subsidisation' rather than on market forces.<sup>7</sup> This increase in use of subsidies created such trade distortions that the GATT signatories negotiated a Subsidies Code during the Tokyo Round negotiations to regulate the use of subsidies.<sup>8</sup> Yet, this Subsidies Code explicitly recognized that subsidies formed an integral part of economic development. Therefore, an outright ban on subsidies would forbid developing countries 'to assist their industries'.<sup>9</sup>

Thus, although the Subsidies Code attempted to minimize the trade distortive effects of subsidies, it proved unsuccessful as the issue of subsidization coincided with the recession of the early 1980s. This added pressure on countries to support their domestic industries leading to further

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<sup>4</sup> The United Nations Economic and Social Council, Report of the First Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, 8, 16, 17, 32, E/PC/33 (1946). See also, Robert E. Baldwin, *Imposing Multilateral Discipline on Administered Protection* in *THE WTO AS AN INTERNATIONAL ORGANIZATION* 297-327, 86 (Anne O. Krueger ed., University of Chicago Press 1998).

<sup>5</sup> Summary Record of the Seventeenth Meeting, 11, the GATT Contracting Parties Ninth Session, SR.9/17, (1954); See also, Dominic Coppens, *WTO DISCIPLINES ON SUBSIDIES AND COUNTERVAILING MEASURES – BALANCING POLICY SPACE AND LEGAL CONSTRAINTS* 23-24 (Cambridge University Press 2014).

<sup>6</sup> Report of the Director-General of GATT, the Tokyo Round of Multilateral Trade Negotiations, 53 (1979).

<sup>7</sup> *THE GATT URUGUAY ROUND – A NEGOTIATING HISTORY (1986-1992) VOLUME I: COMMENTARY* 817 (Terence P. Stewart ed., Kluwer Law and Taxation Publishers, 1993) [hereinafter 'Stewart, THE GATT URUGUAY ROUND'].

<sup>8</sup> Preamble, Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade ("Subsidies Code") [hereinafter 'Subsidies Code'].

<sup>9</sup> Articles 14:1 and 14:2 of the Subsidies Code.

subsidization.<sup>10</sup> In 1985, a Preparatory Committee was established for the Uruguay Round to address the issue of subsidies.<sup>11</sup> In particular, the US wanted to address strategies put in place by certain countries that were using bundles of subsidies in order to enable their domestic industry to reach market dominance and become global players in specific sectors.<sup>12</sup> The subject of the subsidies negotiations in the Uruguay Round was thus focussed on curtailing the use of subsidies by states for the purposes of enhancing their domestic industry, so as to avoid subsidy races.<sup>13</sup> Consequently, as explained by the WTO Expert Group on Trade Financing, the SCM Agreement 'is in general drafted to address situations where a WTO Member is subsidizing the production or sale of its own goods.'<sup>14</sup>

However, with globalization and an increasingly interconnected world, subsidies have become less domestically focused. It has become common to encounter situations of subsidization that have transnational elements. Export buyer insurance and export buyer credit are examples of such instances that have become widely used, whereby the government of the exporting producer subsidizes foreign purchasers of that exporting producer's goods. For example, in the *Brazil – Aircraft* dispute, Canada alleged that a Brazilian export financing program was granting support to foreign buyers of a Brazilian aircraft manufacturer.<sup>15</sup> Similarly, the rise of large European companies led to subsidies given by one European Member State to companies located in other EU Member States, which has been the case for several of the challenged subsidy schemes at the WTO in the *EC – Large Civil Aircraft* dispute.

In the same way, the growth of global value chains may lead to various scenarios in which subsidies have a transnational element, as governments may subsidize a company in their own country which may, by extension, subsequently use this subsidy for production in several other countries. This issue arose, for example, in a US investigation where a French steel company that had production operations in several countries wanted the subsidies it received from the French government to be allocated over its worldwide production.<sup>16</sup> Another scenario that has also become increasingly common is where an input supplier is subsidized by its own government, but the supplier exports this input for production to another country, which in turn, exports the final good to its final country of destination.

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<sup>10</sup> Stewart, THE GATT URUGUAY ROUND, *supra* note 7 at 821-833. George Kleinfeld and David Kaye, *Red Light, Green Light? The 1994 Agreement on Subsidies and Countervailing Measures, Research and Development Assistance, and US Policy*, 28(6) JOURNAL OF WORLD TRADE 43, 43 (1994). [hereinafter 'Kleinfeld and Kaye, *Red Light, Green Light?*'].

<sup>11</sup> Trade Policies for a Better Future, 'The Leutwiler Report', the GATT and the Uruguay Round 139 (1987).

<sup>12</sup> *Communication from the United States*, Multilateral Trade Negotiations – The Uruguay Round Negotiating Group on Subsidies and Countervailing Measures, 3, MTN.GNG/NG10/W/1 (1987); *Communication from the United States*, Multilateral Trade Negotiations – The Uruguay Round Negotiating Group on Subsidies and Countervailing Measures, 4, MTN.GNG/NG10/W/20 (1988) [hereinafter 'US Communication in MTN']; *Elements of the Framework for Negotiations – Submission by the United States*, Multilateral Trade Negotiations – The Uruguay Round Negotiating Group on Subsidies and Countervailing Measures, 1, MTN.GNG/NG10/29 (1989).

<sup>13</sup> *Id.* US Communication in MTN at 4; Americo Beviglia Zampetti, *The Uruguay Round Agreement on Subsidies – A Forward Looking Assessment*, 29(6) JOURNAL OF WORLD TRADE 5, 8 (1995).

<sup>14</sup> THE WORLD TRADE ORGANIZATION, *Expert Group Meeting on Trade Financing – Note by the Secretariat*, General Council Working Group on Trade, Debt and Finance, 5, WT/GC/W/527 (2004) [hereinafter 'Expert Group Meeting on Trade Financing 2004'].

<sup>15</sup> Panel Report, *Brazil – Export Financing Programme for Aircraft*, WT/DS46/R (1999) [hereinafter 'PR, *Brazil – Aircraft*'].

<sup>16</sup> *Usinor Sacilor v. United States*, 991 F. Supp. 665 (the US CIT 1997).

## 1.2. Transnational subsidies under the BRI

Notwithstanding the abovementioned scenarios, it is undeniable that under the BRI and its ‘going out’ policy, China is changing the way in which subsidies may have a transnational element. Indeed, one of the main short-term aims of the BRI is to alleviate industrial excess capacity in China by assisting Chinese companies to move abroad.<sup>17</sup>

While new investment vehicles have been created to conduct financing under the BRI, such as the Silk Road Fund, most of the funding comes from Chinese state-owned banks or commercial banks.<sup>18</sup> This financing covers not only infrastructure projects, but also assistance to Chinese companies relocating in third countries. As explained by the Premier of China in 2014, ‘[w]e encourage competitive Chinese producers of iron and steel, cement and plate, etc. to shift their operation to ASEAN countries to meet the local need of infrastructure development through investment, leasing and loan lending so as to achieve mutual benefit’.<sup>19</sup> The introduction of a ‘polluter-payer’ mechanism in China has also reduced profits in highly polluting industries, which has given Chinese producers an incentive to move production abroad.<sup>20</sup>

As a result, Chinese state-owned banks such as China EXIM Bank, the Agricultural Development Bank of China, the Bank of China or SINOSURE have been providing financing in the forms of loans, export guarantees and export insurance to Chinese companies establishing themselves outside China.<sup>21</sup>

In addition to financing to Chinese companies establishing production in third countries, Chinese development firms have started operating many special economic zones alongside the BRI modelled after the Shenzhen Special Economic Zone in China. Much of China’s foreign investment is flooded into these zones. They have been described as Chinas “preferred mode of economic expansion” bringing along many Chinese workers with them.<sup>22</sup> These industrial parks are meant to become a place for Chinese firms to establish themselves abroad by providing infrastructure, utility services or assisting them in their dealings with local authorities.<sup>23</sup>

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<sup>17</sup> OECD, *China’s Belt and Road Initiative in the Global Trade, Investment and Finance Landscape*, OECD Business and Finance Outlook, 3 (2018) <<https://www.oecd.org/finance/Chinas-Belt-and-Road-Initiative-in-the-global-trade-investment-and-finance-landscape.pdf>> [hereinafter ‘OECD, *China’s BRI in the Global Trade*’].

<sup>18</sup> *Id.*

<sup>19</sup> China-ASEAN Business Council, ‘Remarks by Chinese Premier Li Keqiang at the 17th ASEAN-China Summit’, 13 November 2014, <<http://www.china-aseanbusiness.org.cn/index.php?m=content&c=index&a=show&catid=37&id=16457>>

<sup>20</sup> See Dirk van der Kley, *China shifts polluting cement to Tajikistan*, Chinadialogue, 8 August 2016 <<https://www.chinadialogue.net/article/show/single/en/9174-China-shifts-polluting-cement-to-Tajikistan>>

<sup>21</sup> OECD, *China’s BRI in the Global Trade*, *supra* note 17 at 18-19.

<sup>22</sup> Viva Laos Vegas, *South-East Asia is sprouting Chinese Enclaves*, THE ECONOMIST, 30 January 2020, <<https://www.economist.com/asia/2020/01/30/south-east-asia-is-sprouting-chinese-enclaves>> [hereinafter “Vegas, *South-East Asia is Sprouting Chinese Enclaves*”].

<sup>23</sup> HSBC, *Industrial zones under the BRI*, <<https://www.business.hsbc.com/belt-and-road/industrial-zones-under-the-bri>>

### 1.3. Complaints brought to the Commission

These new developments have led to a number of complaints filed before the Commission in 2019.

In April 2019, the Commission received a complaint to initiate an anti-subsidy investigation against import of glass fibre fabrics originating from both China and Egypt. Interestingly, the complainants alleged that the producers in Egypt are located in a special economic zone set up under an agreement between the governments of China and Egypt and are controlled by a Chinese government agency to foster China's outward expansion.<sup>24</sup> The complainants contended that the producers in Egypt benefit from 'financial contributions granted indirectly via Chinese government-owned or controlled banks or other Chinese state-owned or state-controlled entities (directly or via Egyptian entities) to foster foreign investment in the special economic zones by virtue of the agreements between the Chinese and Egyptian governments.'<sup>25</sup> Based on this complaint, the Commission initiated an anti-subsidy investigation in May 2019.<sup>26</sup>

Soon after this first complaint, the Commission received another complaint concerning imports of glass fibre products, but this time originating solely from Egypt. Based on this complaint, the Commission initiated an anti-subsidy investigation in July 2019. In the notice of initiation, it indicated that the complainant alleged that the producers benefited from subsidies granted directly by the Government of Egypt or via Egyptian entities in the context of the cooperation between Egypt and China to foster investments in a special economic zone. The Commission added that the complaint contains evidence of the cooperation agreements between the Chinese and the Egyptian Governments as well as loans from Chinese state-owned or state-controlled entities to Egyptian state-owned banks.<sup>27</sup>

Finally, in October 2019, the Commission received yet another complaint – this time regarding imports of hot rolled stainless steel sheets and coils from China and Indonesia. In the summary of the complaint, the complainants highlight that the Government of Indonesia has 'actively given preferential treatment for the establishment of Indonesian subsidiaries of the Chinese SSHR [stainless steel hot-rolled flat products] producers by complementing financing provided by China' and that the Government of China has subsidized the "going out" of the Chinese SSHR industry under the joint perspective of offshoring domestic excess capacity and seizing opportunities along the "One Belt and One Road" initiative [BRI].'<sup>28</sup> The Commission further explained in the notice of

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<sup>24</sup> Executive Summary of the Complaint under Article 10 of Regulation 2016/1037 Concerning Continuous Filament Glass Fibre Fabrics from China and Egypt <[https://trade.ec.europa.eu/tdi/case\\_details.cfm?id=2398&publication=2661&action=readfile](https://trade.ec.europa.eu/tdi/case_details.cfm?id=2398&publication=2661&action=readfile)> (last accessed on 25 January 2020).

<sup>25</sup> *Id.* at 3.

<sup>26</sup> Notice of Initiation of an Anti-Subsidy Proceeding Concerning Imports of Certain Woven and/or Stitched Glass Fibre Fabrics Originating in the People's Republic of China and Egypt, OJ 2019 C 167/11.

<sup>27</sup> Notice of initiation of an Anti-subsidy proceeding Concerning Imports of Continuous Filament Glass Fibre Products Originating in Egypt, OJ 2019 C 192/30.

<sup>28</sup> Request for the Initiation of an Anti-Subsidy Investigation Concerning Imports of *Hot Rolled Stainless Steel Sheets And Coils* Originating in Indonesia and the People's Republic of China, Executive Summary of the Complaint, <[https://trade.ec.europa.eu/tdi/case\\_details.cfm?id=2420&publication=2772&action=readfile](https://trade.ec.europa.eu/tdi/case_details.cfm?id=2420&publication=2772&action=readfile)> (last accessed on 25 January 2020).



initiation that the complainant alleged that some of the subsidies were directly provided by the Government of China.<sup>29</sup>

Interestingly, in the first investigation, the Commission does not seem to engage with the allegations of transnational subsidisation put forth by the complainants as the notice of initiation of that case only indicates that there could be potential subsidisation 'indirectly by the Government of China, but via the Government of Egypt'.<sup>30</sup> However, in the second investigation, the Commission went a step further to mention that there could be subsidization 'via Egyptian entities in the context of the cooperation between Egypt and the People's Republic of China',<sup>31</sup> thereby considering indirect subsidization from the Government of China without possible involvement of the Government of Egypt. In the third investigation, the Commission took yet another step to acknowledge allegations that 'the subsidies are directly granted by the Government of Indonesia, and some by the Government of China',<sup>32</sup> thus clearly mentioning transnational subsidies for the first time.

The complaints against financing from Chinese banks are understandable as such financing is typically found to be a subsidy provided by the Government of China to its domestic producers in anti-subsidy investigations. Similarly, the fact that Chinese producers establish their foreign subsidiaries in special economic zones may raise questions regarding the price paid for land or utility services. Thus, the pertinent question is whether the geographical location of the recipient of the subsidy alters the conclusion that this financing and assistance may be considered a subsidy under the SCM Agreement. Indeed, in the words of the Expert Group on Trade Financing, 'it is not entirely clear whether or not the [SCM Agreement] applies where the subsidizing entity is not within the territory of the Member whose goods are allegedly being subsidized'.<sup>33</sup>

## **2. Transnational subsidies under the SCM Agreement**

In the usual subsidization scenario, a government grants a financial contribution which confers a benefit to a producer located within its territory.<sup>34</sup> Until recently, the idea that a government could subsidize a producer outside of its territory was discarded as 'unrealistic'.<sup>35</sup> The result is that the SCM Agreement does not cover this situation explicitly. While Article 1 of the SCM Agreement does not impose any clear limitation regarding the location of the recipient of the subsidy (Section 3.1 and 3.2), Article 2 and footnote 63 appear to impose limitations regarding the location of the possible recipients of the subsidy, except perhaps for prohibited subsidies under Article 3 (Section 3.3). This preliminary

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<sup>29</sup> The European Commission, Notice of Initiation of an Anti-Subsidy Proceeding Concerning Imports of Certain Hot Rolled Stainless Steel Sheets and Coils Originating in the People's Republic of China and Indonesia, OJ 2019 C 342/18.

<sup>30</sup> The European Commission, Notice of Initiation of an anti-subsidy proceeding concerning imports of certain woven and/or stitched glass fibre fabrics originating in the People's Republic of China and Egypt, 16 May 2019, O. 2019 (C 167) 11.

<sup>31</sup> The European Commission, Notice of Initiation of an Anti-Subsidy Proceeding Concerning Imports of Continuous Filament Glass Fibre Products Originating in Egypt, OJ 2019 C 192/30.

<sup>32</sup> The European Commission, Notice of Initiation of an anti-Subsidy Proceeding Concerning Imports of Certain Hot Rolled Stainless Steel Sheets and Coils Originating in the People's Republic of China and Indonesia, OJ 2019 C 342/18.

<sup>33</sup> Expert Group Meeting on Trade Financing 2004, *supra* note 14 at 5.

<sup>34</sup> *Id.*

<sup>35</sup> Benitah, SUBSIDIES, *supra* note 2 at 605.

conclusion that the recipient of the subsidy needs to be in the territory of the subsidizing Member is further confirmed by other provisions of the SCM Agreement (Section 3.4).

## **2.1. Recipient of the ‘financial contribution’ by a ‘government or a public body’**

Article 1.1(a)(1) of the SCM Agreement reads that ‘there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as “government”)’ so that it seems to impose a territorial limitation on the location of the government granting the subsidy but not on the financial contribution. On the other hand, Article 1.1(a)(1)(iv) of the SCM Agreement, which indicates that a subsidy can be granted indirectly via a private body if that body is entrusted or directed by a government, does not appear to impose any restriction regarding the location of the entrusted or directed private body.

The qualifier term ‘within the territory of a Member’ in Article 1.1(a)(1) only refers to ‘government or a public body’ and does not concern the term ‘financial contribution’. The qualifier does not indicate where the recipient of the financial contribution must be located. This is because the qualifier follows the term ‘a government or any public body’ directly and because the term ‘by a government or any public body’ is not between commas. This interpretation is further confirmed by the insertion immediately after the definition of ‘government’ between brackets, which clarifies the term to mean ‘a government or any public body within the territory of a Member’.<sup>36</sup>

In *US – FSC (Article 21.5 DSU)*, the US was asked by the panel whether a measure by a Member provided for the production of a good outside the territory of that Member can be a ‘subsidy’ under Article 1 of the SCM Agreement.<sup>37</sup> While this question was ultimately not ruled upon by the panel, the US’ response clarified that ‘the recipient of a financial contribution need not be within the territory of that Member. If the latter had been intended, the provision presumably would have read “a financial contribution within the territory of a Member by a government”’.<sup>38</sup> This was also the understanding of the parties in the *Brazil – Aircraft* dispute where Brazil and Canada agreed that export financing payments were a financial contribution by the Brazilian Government to foreign aircraft buyers.<sup>39</sup>

As a result, Article 1.1(a)(1) of the SCM Agreement indicates that the government or public body granting the financial contribution needs to be located within the territory of a WTO Member. It does not impose any restriction regarding the location of an entrusted or directed private body or of the recipient of the financial contribution.

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<sup>36</sup> Panel Report, *United States - Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, para. 8.67, WT/DS379/R, (2010). [hereinafter ‘PR, US — Anti-Dumping and Countervailing Duties (China)’].

<sup>37</sup> Panel Report, *United States - Tax Treatment for "Foreign Sales Corporations" - Recourse to Article 21.5 of the DSU by the European Communities*, Annex F-1 in question 43 and Annex F-3 in question 43, WT/DS108/RW (2001). [hereinafter ‘PR, US – FSC (Art. 21.5 DSU)’].

<sup>38</sup> *Id.* at Annex F-3 in para. 103. The EC however seemed to disagree at that time as it clarified that while there was no limitation on the recipient of the benefit, the recipient of the financial contribution should be within the territory of a Member, see Annex F-1, para. 155.

<sup>39</sup> PR, *Brazil – Aircraft*, *supra* note 15 at paras. 2.1-2.6 and 4.19-4.20.

## 2.2. Recipient of the ‘benefit’

Article 1.1(a)(2) simply indicates that ‘a benefit is thereby conferred’. While this Article does not impose any territorial limitation regarding the location of the recipient of the benefit, it is relevant to find who the recipient of the benefit is. It is this recipient that will define the recipient of the subsidy throughout the SCM Agreement.

As explained by the Appellate Body (**AB**), ‘[t]he SCM Agreement does not include a specific definition of the “recipient” of a “benefit”’.<sup>40</sup> However, the recipient of the benefit needs to be ‘the producer of the exported goods subject to the countervailing investigation’.<sup>41</sup> This recipient of the benefit can be different from the recipient of the financial contribution. Indeed, a “financial contribution” and a “benefit” [are] two separate legal elements in Article 1.1 of the SCM Agreement, which together determine whether a subsidy exists’.<sup>42</sup> As the same financial contribution can confer a benefit to one or more distinct persons,<sup>43</sup> and the benefit does not necessarily have to flow directly from the financial contribution,<sup>44</sup> it is important to assess which is the producer to which the financial contribution grants a benefit. It is this producer which will define the recipient of the subsidy itself.<sup>45</sup>

For example, in the case of buyer export credits, a subsidy is not defined in terms of benefit to the buyers but in terms of benefit to the exporting producers from whom the buyer purchased.<sup>46</sup> To this end, in the *Brazil – Aircraft* dispute, Brazil and Canada agreed that export financing payments were a direct transfer of funds by the Brazilian Government to foreign aircraft buyers but that the benefit was to be assessed based on the situation of the Brazilian aircraft producer.<sup>47</sup> This reasoning was further confirmed in *Brazil – Aircraft (Article 21.5 DSU – Canada II)*, where Canada had to establish that the ‘payments confer a benefit on the producers of that product’ and the relevant question before the panel was whether the export credit support was benefiting the Brazilian exporter.<sup>48</sup>

As a result, Article 1.1(b) does not limit the location of the recipient of the benefit. However, the recipient of the benefit is relevant as it is this recipient which defines the recipient of a subsidy under the SCM Agreement.<sup>49</sup>

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<sup>40</sup> Appellate Body Report, *United States — Countervailing Measures Concerning Certain Products from the European Communities*, para. 112, WT/DS212/AB/R (2002). [hereinafter ‘ABR, US — Countervailing Measures on Certain EC Products’].

<sup>41</sup> Panel Report, *Canada - Measures Affecting the Export of Civilian Aircraft - Report of the Panel*, para. 7.54, WT/DS70/R (1999).

<sup>42</sup> Appellate Body Report, *Brazil – Export Financing Programme for Aircraft*, para. 157, WT/DS46/AB/R (1999)

<sup>43</sup> ABR, US — Countervailing Measures on Certain EC Products, *supra* note 40 at para. 110.

<sup>44</sup> *Id.*

<sup>45</sup> See Art. 14, Agreement on Subsidies and Countervailing Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 14 [hereinafter ‘SCM Agreement’].

<sup>46</sup> PR, *Brazil – Aircraft*, *supra* note 15 paras. 4.40-4.48.

<sup>47</sup> *Id.* at paras. 2.1-2.6, 4.19-4.20 and 4.40-4.48. Note that the EC seemed to have a different understanding of this case, see PR, *US – FSC (Art. 21.5 DSU)*, *supra* note 37 at Annex F-3, para. 110.

<sup>48</sup> Panel Report, *Brazil - Export Financing Programme for Aircraft - Second Recourse by Canada to Article 21.5 of the DSU*, footnote 42, WT/DS46/RW2 (2001).

<sup>49</sup> See also on this point, PR, *US – FSC (Art. 21.5 DSU)*, *supra* note 37 at Annex F-3 in para. 109.

### 2.3. Limitation on location of the recipient of the subsidy

While Article 1.1 of the SCM Agreement does not impose any specific requirement on the location of the recipient of the subsidy, the location of the recipient of the subsidy appears to be limited by the definition of specificity and by the guidelines to calculate the amount of subsidization, at least regarding non-prohibited subsidies under Article 3 of the SCM Agreement.

#### 2.3.1. Specificity

As mentioned, Article 1.2 of the SCM Agreement indicates that a subsidy needs to be specific in accordance with the provisions of Article 2. Article 2 of the SCM Agreement clearly states that to be 'specific', a subsidy needs to be given to an enterprise or industry or group of enterprises or industries 'within the jurisdiction of the granting authority' except if that subsidy is a prohibited subsidy under Article 3. Thus, if the subsidy is not covered by Article 3, the possible recipients of the subsidy need to be 'within the jurisdiction of the granting authority'.

According to the AB, the assessment of 'jurisdiction' and 'granting authority' involves a holistic analysis and must be done in a conjunctive manner as these two are interlinked.<sup>50</sup> The AB also explained that the identification of the jurisdiction of the granting authority is informed by whether the financial contribution was provided by the 'government', by 'any public body within the territory of a Member', or by a 'private body' entrusted or directed by the government.<sup>51</sup>

The use of the term 'granting authority' in Article 2 instead of 'government', as defined in Article 1, suggests that 'the granting authority' might differ from the central government of the subsidizing Member.<sup>52</sup> 'Authority' is defined as 'a person or (esp.) body having political or administrative power and control in a particular sphere; the body or bodies held responsible for enforcing law and order, providing public services, etc., in a country or region'.<sup>53</sup> However, not all financial contributions are performed by bodies which hold the power to regulate.<sup>54</sup> This is, for example, the case of the Chinese state-owned banks or private bodies which are entrusted or directed by the government. Therefore, how should 'the jurisdiction of the granting authority' be assessed in such cases?

In situations in which a body that does not have regulatory powers grants a subsidy, it is thus necessary to assess which governmental authority is behind that body to determine the granting

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<sup>50</sup> Appellate Body Report, *United States — Definitive Anti-Dumping and Countervailing Duties on Certain Products from China*, para. 4.168, WT/DS379/AB/R (2011). [hereinafter 'ABR, US — Anti-Dumping and Countervailing Duties (China)'].

<sup>51</sup> *Id.* at para. 4.167.

<sup>52</sup> Appellate Body Report, *United States — Measures Affecting Trade in Large Civil Aircraft — Second Complaint*, paras. 750-756 and fn 1570, WT/DS353/AB/R (2012) [hereinafter 'ABR, US — Large Civil Aircraft (2<sup>nd</sup> Complaint)']; PR, *US — Anti-Dumping and Countervailing Duties (China)*, *supra* note 36 at para. 7.247.

<sup>53</sup> Oxford English Dictionary, definition of 'Authority' <<https://www.oed.com/start;jsessionid=CD3EB7B59F69FD2A97FD60813BD3FF29?authRejection=true&url=%2Fview%2FEntry%2F13349%3FredirectedFrom%3Dauthority#eid>>

<sup>54</sup> Appellate Body Report, *United States — Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India*, para. 4.17, WT/DS436/AB/R (2014).

authority for the purpose of Article 2. In case a private body is entrusted or directed, it will generally be the government that gives responsibility to or exercises its authority over this private body,<sup>55</sup> whereas for a public body, this will be the governmental authority that vested this public body with governmental authority.<sup>56</sup> In this regard, subsidies granted by bodies that do not have regulatory powers will often be granted under ‘subsidy programmes’. For example, in *US — Anti-Dumping and Countervailing Duties (China)* it was confirmed that preferential lending by Chinese state-owned banks was granted pursuant to a ‘number of central, provincial, and municipal laws, plans and policies such as the “11th Five-Year Plan (2006-2010)”’.<sup>57</sup> In such situations, it is the jurisdiction of the authority in charge of the subsidy program, instead of the body performing the financial contribution itself, that needs to be assessed as it is this governmental authority that is behind the granting body.<sup>58</sup> As a result, it is the ‘authority’, whose relationship with the public or private body performing the financial contribution gives rise to regulatory attribution, which will be the granting authority for the purpose of Article 2 of the SCM Agreement.

In case of financing from Chinese state-owned banks and the provision of infrastructure or public services by Chinese special economic zones to Chinese companies established in a third country, the granting authority is thus the authority that gives rise to regulatory attribution to these bodies. Regarding Chinese state-owned banks, this is the central government of China. With regard to the economic zones, in the complaint submitted to the Commission in *Hot rolled stainless steel sheets and coils (China, Indonesia)*, the complainants allege that this support is granted under the “going out” of the Chinese SSHR industry and the “One Belt and One Road” initiative’. As these policies are adopted by the central Government of China, it is this authority as well that gives rise to regulatory attribution in this scenario.

Regarding the term ‘within the jurisdiction’, there has been little discussion in WTO jurisprudence. ‘Jurisdiction’ is defined as ‘[t]he extent or range of judicial or administrative power; the territory over which such power extends’.<sup>59</sup> The US in *US – FSC (Article 21.5 DSU)* agreed with this definition when it explained that, for a taxation subsidy, ‘jurisdiction’ refers to the tax jurisdiction of the WTO Member.<sup>60</sup> This is line with the understanding of state jurisdiction under international law as ‘the power of a state under international law to regulate or otherwise impact upon people, property and

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<sup>55</sup> Appellate Body Report, *United States — Anti-Dumping Duty on Dynamic Random Access Memory Semiconductors (DRAMs) of One Megabit or Above from Korea*, para. 116. WT/DS296/AB/R (2005).

<sup>56</sup> PR, *US — Anti-Dumping and Countervailing Duties (China)*, *supra* note 36 at paras. 5.95-5.103.

<sup>57</sup> ABR, *US — Anti-Dumping and Countervailing Duties (China)*, *supra* note 50 at paras. 381 and 385. Also see, with regard to the provision of inputs for less than adequate remuneration, PR, *US — Anti-Dumping and Countervailing Duties (China)*, *supra* note 36 at para. 7.242.

<sup>58</sup> Panel Report, *United States — Continued Dumping and Subsidy Offset Act of 2000*, para. 7.113-7.114, WT/DS217/R (2002).

<sup>59</sup> Oxford English Dictionary, definition of ‘jurisdiction’

<<https://www.oed.com/start?authRejection=true&url=%2Fview%2FEntry%2F102156%3FredirectedFrom%3Djurisdiction#eid>> [hereinafter ‘*Jurisdiction*, Oxford English Dictionary’].

<sup>60</sup> PR, *US – FSC (Art. 21.5 DSU)*, *supra* note 37 at Annex F-3 in para. 108.

circumstances'.<sup>61</sup> As explained in the *Lotus* case, the jurisdiction of a State 'is certainly territorial; it cannot be exercised by a State outside its territory'.<sup>62</sup>

This territorial interpretation of jurisdiction is in line with the views taken by the AB.<sup>63</sup> The SCM Agreement's legislative history also confirms it. At a meeting of the Negotiating Group on Subsidies and Countervailing Measures, '[i]t was proposed to clarify that specificity may exist only within the territory of a signatory'.<sup>64</sup> Article 2.1 of the draft SCM Agreement was thus amended so that for a subsidy to be specific it had to be granted to enterprises 'within the territory of the subsidizing country'.<sup>65</sup> Article 2.1 was however subsequently amended together with Article 2.2 at the request of Canada because read together, these Articles 'deemed any subsidy offered by a provincial government in Canada to be specific even if it was generally available throughout the province'.<sup>66</sup> As a result, both Articles were amended to mention the term 'within the jurisdiction of the granting authority'.

It is however possible to derogate from the principle that jurisdiction is territorial 'by virtue of a permissive rule derived from international customs or from a convention'.<sup>67</sup> A rare example of such an agreement is the treaty between Netherlands, the United Kingdom (**UK**) and Northern Ireland concerning a Scottish trial in the Netherlands which permitted the trial of the Lockerbie subjects by a Scottish Court according to Scottish law in Dutch territory.<sup>68</sup> Such situations also occur where a state grants sovereignty over part of its territory to another state such as with the UK's military bases in Cyprus or where a state grants *de facto* control over its territory such as with Guantanamo Bay in Cuba.<sup>69</sup> An example of a situation whereby a state claims rights over foreign territory based on customs was the *Rights of Passage Case (Portugal v India)* where it was acknowledged that right of passage between Portugal's enclave territories in India could exist on the basis of customary law.<sup>70</sup>

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<sup>61</sup> Malcolm N. Shaw, *INTERNATIONAL LAW*, 469 (7<sup>th</sup> ed. Cambridge University Press 2014).

<sup>62</sup> S.S. "Lotus", France v Turkey, Judgment, (1927), para 45, PCIJ Series A no 10, ICGJ 248 (PCIJ 1927), 7th September 1927.

<sup>63</sup> For example, AB in *US – Shrimp*, found that a US import ban on shrimp harvested in a way harmful to sea turtles had a nexus with the US territory as sea turtles traversed US waters. See, Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, para. 133, WT/DS58/AB/R (1998).

<sup>64</sup> Meeting of 6 November 1990, Note by the Secretariat, Negotiating Group on Subsidies and Countervailing Measures, para. 3, MTN/GNG/NG10/24 (29 November 1990).

<sup>65</sup> Draft Final Act Embodying the results of the Uruguay Round of Multilateral Trade Negotiations, Trade Negotiations Committee, I.2, MTN.TNC/W/FA (20 December 1991).

<sup>66</sup> Trade Negotiations Committee: Thirty-Third Meeting, Trade Negotiations Committee, para. 25, MTN.TNC/37 (29 November 1993).

<sup>67</sup> *Lotus Case*, *supra* note 62 at para. 45.

<sup>68</sup> Agreement between the Government of the Kingdom of the Netherlands and the Government of the United Kingdom of Great Britain and Northern Ireland concerning a Scottish trial in the Netherlands, 38(4) ILM 926-936 (1999).

<sup>69</sup> Martin Dixon, *INTERNATIONAL LAW* 150 (7<sup>th</sup> ed., Oxford University Press 2013).

<sup>70</sup> *Rights of Passage Case (Portugal v India)* 1960] ICJ Rep 6, ICGJ 174 (ICJ 1960), 12th April 1960, International Court of Justice [ICJ]; See also *The North Atlantic Coast Fisheries Case*, Great Britain v United States, Award, (1961) XI RIAA 167, (1910) 4 AJIL 948, ICGJ 403 (PCA 1910), 7th September 1910, Permanent Court of Arbitration [PCA]; and the *SS 'Wimbledon'*, United Kingdom and Ors v Germany, Judgment, (1923) PCIJ Series A no 1, ICGJ 235 (PCIJ 1923), 17th August 1923, PCIJ.

In this regard, as companies established in third countries are located outside the territory of China and have the nationality of their place of establishment regardless of their shareholding,<sup>71</sup> the only logical conclusion is that these producers established in third countries are not within the jurisdiction of the Government of China. The fact that these Chinese companies may have been established within special zones set up under agreements between the Government of China and the host country would hardly alter this conclusion, unless the government of the host country has effectively granted to China the right to make its laws applicable and to enforce them within these zones.

This conclusion might however differ if the financing and provision of services to these companies were found to be prohibited subsidies under Article 3, as the requirement that they be located within the jurisdiction of the Government of China would then not be applicable.

### 2.3.2. Calculation of the amount of the subsidy to the recipient

Footnote 63 to paragraph 2 of Annex IV of the SCM Agreement confirms the conclusion that, at least with regard to non-prohibited subsidies, the recipient of the subsidy needs to be within the territory of the subsidizing Member. This footnote, which establishes guidelines for the calculation of the total *ad valorem* subsidization under Article 6.1(A), indicates that '[t]he recipient firm is a firm in the territory of the subsidizing Member.'

While this footnote has never been discussed by a panel or the AB, the US in a reply to a panel question in *US – FSC (Article 21.5 DSU)* explained that

*[o]ne can interpret this footnote two different ways. One interpretation is that it simply restates what is assumed in the remainder of the SCM Agreement; i.e., that the recipient of a subsidy must be located within the territory of the subsidizing Member. Another interpretation, however, is that this footnote is necessary because it is not assumed in the remainder of the Agreement that the recipient must be located within the territory of the subsidizing Member.*<sup>72</sup>

Contrary to what the US stated in that dispute,<sup>73</sup> the former interpretation seems more logical. Indeed, footnote 63 is necessary to make sure that the total *ad valorem* subsidization is calculated solely based on the value of the sales of the producer in the territory of the subsidizing Member without including possible sales of its related producing and selling entities in third countries. Moreover, as discussed above, the same financial contribution can confer a benefit to more than one entity such as in the case of buyer export credits or insurance. In such a case, footnote 63 clarifies that the amount of subsidization needs to be calculated based on the sales of the firm receiving the benefit in the subsidizing Member. Furthermore, it would be contradictory to have different definitions of a

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<sup>71</sup> One of the main exceptions to the principle of territoriality of prescriptive jurisdiction is the principle of nationality. In *Barcelona Traction*, the International Court of Justice expressly rejected that a state can exercise jurisdiction over a company because of the nationality of that company's shareholders and insisted that a state's jurisdiction is defined by a company's state of incorporation. See, *Barcelona Traction, Light and Power Company Limited (New Application, 1962)*, *Belgium v Spain*, Judgment, Merits, Second Phase, ICJ GL No 50, [1970] ICJ Rep 3, (1970) 9 ILM 227, ICGJ 152 (ICJ 1970).

<sup>72</sup> PR, *US – FSC (Art. 21.5 DSU)*, *supra* note 37 at Annex F-3 in para. 107.

<sup>73</sup> *Id.*

‘recipient’ for the purpose of calculating the amount of the subsidy regarding serious prejudice under Article 6.1(a) and for determining whether a subsidy exists. In any case, the fact that footnote 63 applies to the determination of serious injury for actionable subsidies implies that, at least with regard to subsidies which are not prohibited under Article 3, the recipient of the benefit needs to be located within the territory of the subsidizing Member.

## **2.4. Other relevant provisions**

Other provisions of the SCM Agreement also confirm that the exporting Member cannot be perceived separately from the subsidizing Member under the SCM Agreement, at least for non-prohibited subsidies.

### *Subsidizing Member’s rights*

Article 13 of the SCM Agreement clarifies that as soon as an anti-subsidy complaint is accepted, the investigating authority needs to invite for consultations the Member, ‘the products of which may be subject to such investigation’. Still, in accordance with Article 13, this Member should be afforded a reasonable opportunity to continue consultations and shall be granted access to non-confidential evidence. Similarly, regarding undertakings, Article 18 envisages the possibility that the ‘government of the exporting Member agrees to eliminate or limit the subsidy or take other measures concerning its effects’. By granting these rights solely to the exporting Member, the SCM Agreement indicates that the subsidizing Member and the exporting Member should normally be one and the same.

### *Countermeasures*

While Article 7 of the SCM Agreement would technically not prevent the importing Member from requesting consultations with the subsidizing Member directly without involving the exporting Member and to subsequently request the establishment of a panel, it seems difficult to see how retaliation, in the form of countermeasures, could take place under Article 7.9. Indeed, in this situation, the adverse effects would not directly be caused by imports from the subsidizing Member, but by those of the exporting Member, so that it is unclear whether the importing Member could retaliate directly against the subsidizing Member.

### *Benchmark*

Similarly, with regard to the calculation of the amount of the subsidy, Article 14(a) indicates that a ‘government provision of equity capital shall not be considered as conferring a benefit, unless the investment decision can be regarded as inconsistent with the usual investment practice [...] of private investors in the territory of that Member’. In this regard, countervailing transnational subsidies would also raise difficulties regarding the benchmark to be taken to calculate the amount of benefit.

### *Notification*

On the other hand, Article 25.2 of the SCM Agreement is clear that WTO Members must only notify subsidies which are specific and ‘granted or maintained within their territories’. The fact that Article 25.2 draws a distinction between specificity and the territory within which the subsidy is granted may



indicate that there could be situations where a subsidy could be specific and granted to an entity outside the subsidizing Member's territory. This would be the case of a prohibited subsidy within the meaning of Article 3, which would be specific by virtue of Article 2.3 of the SCM Agreement despite being granted to a recipient outside the territory of the subsidizing Member.

### 3. Disciplining Subsidies or Allowing Development?

As transnational subsidies do not appear to fall under the ambit of the SCM Agreement, except perhaps for prohibited subsidies under Article 3, it is necessary to consider whether they should nevertheless be disciplined. It is generally accepted that some form of discipline over subsidies is desirable. However, the type and extent of that discipline may vary depending on the type and purpose of the subsidy. Subsidies which have a negative impact on the global commons or that are the most distortive to trade should ideally face a harsher discipline than those that enhance development or address environmental issues, for example.<sup>74</sup> The contradicting aims of curbing trade-distortive subsidies and enhancing development emerges in the context of transnational subsidies and may thus play a role in the appropriate level of discipline that should apply to them.

In this regard, the object and purpose of the SCM Agreement reflect this contradicting aim. On the one hand, as first clarified by the panel in *Brazil – Aircraft*, 'the object and purpose of the SCM Agreement is to impose multilateral disciplines on subsidies which distort international trade.'<sup>75</sup> In *US – Export Restraints*, the panel indicated its concurrence on this, but concluded that not every government action or intervention should be considered as a subsidy that may distort trade. Accordingly, the object and purpose of the SCM Agreement can only be in respect of 'subsidies' as defined in the SCM Agreement, which incorporates the notion of recipient of the benefit and specificity.<sup>76</sup>

On the other hand, the preamble of the Agreement Establishing the WTO clearly indicates that the purpose of this Agreement is to ensure the ability of WTO Members to raise standards of living and ensure their economic development. This purpose is reflected in Part VIII of the SCM Agreement on 'Developing Country Members' and Article 27.1 in particular, which states that '[m]embers recognize that subsidies may play an important role in economic development programmes of developing country Members'. This aim was also expressly mentioned in the preamble of the SCM Agreement's precursor, the Subsidies Code.<sup>77</sup>

Interestingly, with regard to assistance provided by multilateral financial institutions such as the Asian Development Bank, the panel in *EC – Large Civil Aircraft* indicated that it was not clear whether it considered them to be a 'government or any public body within the territory of a Member'. It added

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<sup>74</sup> Gary Horlick & Clarke, *Rethinking Subsidy Disciplines for the Future: Policy Options for Reform*, 20(3) JOURNAL OF INTERNATIONAL ECONOMIC LAW 673, 695 (2017) [hereinafter 'Horlick & Clarke, *Rethinking Subsidies Disciplines*'].

<sup>75</sup> PR, *Brazil – Aircraft*, *supra* note 15 at para. 7.26.

<sup>76</sup> Panel Report, *United States – Measures Treating Export Restraints as Subsidies*, paras. 8.62-8.63, WT/DS194/R (2010).

<sup>77</sup> The SCM Agreement however does not contain a preamble.

that it was important to bear in mind that not all cases of support may involve subsidization that is actionable under the SCM Agreement.<sup>78</sup> Similarly, the Expert Group on Trade Financing explained that

*[m]any WTO Members appeared to be of the view that development aid provided by multilateral development institutions lay outside the scope of ASCM disciplines, or in any event that it would be proper to take action under the Agreement in this context. To date, no Member has challenged multilateral development assistance as a subsidy in WTO dispute settlement proceedings.*<sup>79</sup>

In this regard, Professor Gary Horlick recalls that the term ‘within the territory’ in Article 1 of the SCM Agreement was added following US negotiators’ concerns arising from cases filed in the US in the 1980s, where complainants had claimed that World Bank loans to Brazil, war reparations to Korea by Japan, the Marshall Plan aid, or aid to West Berlin from West Germany should be countervailed.<sup>80</sup> He explains that negotiators did not have the intention to open that ‘can of worms’ as the US was the largest donor of overseas assistance at that time.<sup>81</sup>

A similar analogy may be transposed in the current analysis. The Economist recently questioned the BRI, “what exactly is it? Is it mostly aid or trade? Is it a Chinese Marshall Plan?”<sup>82</sup> With the BRI, China has increasingly assumed the role of being the international and investor for developing countries.<sup>83</sup> However, its objective with the BRI is to provide assistance to developing countries while expanding China’s influence abroad.<sup>84</sup> In this regard, an important aspect of the BRI is that Chinese companies as well as Chinese staff move to third countries.<sup>85</sup>

These differences have created concerns that China has an ‘expansionist’ agenda which should be restrained.<sup>86</sup> In this regard, the fact that Chinese assistance to Chinese-owned companies established outside China has given rise to several complaints filed before the Commission in such a short time is a clear demonstration that China’s ‘going out’ policy is more than a mere assistance

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<sup>78</sup> Panel Report, *European Communities and Certain member States — Measures Affecting Trade in Large Civil Aircraft*, para. 7.888, WT/DS316/R (2010). Note that the panel’s overall reasoning on the meaning of ‘a government or any public body’ was overturned by the AB.

<sup>79</sup> Expert Group Meeting on Trade Financing 2004, *supra* note 15 at 5.

<sup>80</sup> Gary Horlick, An Annotated Explanation of Articles 1 and 2 of the WTO Agreement on Subsidies and Countervailing Measures, 8(9) GLOBAL TRADE AND CUSTOMS JOURNAL 297, 278 (2013). [hereinafter ‘Horlick, *An Annotated Explanation*’].

<sup>81</sup> *Id.*

<sup>82</sup> *China Wants to Put Itself Back at the Centre of the World*, THE ECONOMIST, 6 February 2020, <<https://www.economist.com/special-report/2020/02/06/china-wants-to-put-itself-back-at-the-centre-of-the-world>>

<sup>83</sup> Xi Jinping, *Secure a Decisive Victory in Building a Moderately Prosperous Society in all Respects and Strive for the Great Success of Socialism with Chinese Characteristics for a New Era*, Delivered at the 19th National Congress of the Communist Party of China, 54, 18 October 2017, <[http://www.xinhuanet.com/english/download/Xi\\_Jinping's\\_report\\_at\\_19th\\_CPC\\_National\\_Congress.pdf](http://www.xinhuanet.com/english/download/Xi_Jinping's_report_at_19th_CPC_National_Congress.pdf)>

<sup>84</sup> David Dollar, *Is China’s Development Finance a Challenge to the International Order?* 13 ASIAN ECONOMIC POLICY REVIEW 283, 296 (2018).

<sup>85</sup> Richard Kozul-Wright & Daniel Poon, *China’s Belt and Road isn’t like the Marshall Plan, But Beijing Can Still Learn From It*, SOUTH CHINA MORNING POST 24 January 2019 <<https://www.scmp.com/comment/insight-opinion/united-states/article/2183292/chinas-belt-and-road-plan-isnt-marshall-plan>>

<sup>86</sup> See generally, Horesh Niv, Kim Hyun Jin, Mauch Peter, SUPERPOWER, CHINA? HISTORICIZING BEIJING’S NEW NARRATIVES OF LEADERSHIP AND RESPONSE THERETO (World Scientific, 2014); Monte R. Bullard, The Chinese Expansionist Threat, EAST ASIA PEACE & SECURITY INITIATIVE, 22 February 2019: <<https://www.eapasi.com/blogs1/the-chinese-expansionist-threat>>

and could potentially have trade distortive effects. As China's financing under the BRI is similar to financing that states usually consider as countervailable when granted to China's domestic producers, it is questionable whether such financing should be excluded simply because it is provided to companies established outside China's territory. However, foreign investment has been a major catalyst to development. Developing countries have come to increasingly see foreign investment as a source of economic development, modernization, income growth, and employment.<sup>87</sup> Although often criticized, the BRI does bring employment, tax revenue, and increase infrastructure spending to receiving countries.<sup>88</sup>

Thus, while considering financing under the BRI as a trade distortion that needs to be addressed, one might be tempted by fear of China's hegemony, it may also be seen as a biased Western approach that disregards developing countries' development needs. It follows that while China's cross-border financing is a rising concern, one should be careful to not plainly apply the SCM Agreement's disciplines to transnational subsidies as this might effectively limit the ability of developing countries to enhance their development by attracting foreign companies. In this regard, further thinking on how to best tackle this issue is necessary.

The conclusion that only transnational subsidies qualifying as prohibited subsidies under Article 3 might fall under the SCM Agreement could help bridge this gap. Indeed, prohibited export subsidies are subsidies which are assumed to be highly trade distortive,<sup>89</sup> and by their export-oriented nature, less likely to have development as their primary purpose. As such, by including transnational export subsidies within the ambit of the SCM Agreement, but excluding non-prohibited subsidies from it, an adequate provisional balance could be established between the SCM Agreement's diverging purposes while considering a more adequate way of disciplining transnational subsidies.

#### **4. Domestic Trade Remedy Legislation & Practice**

As explained by the US in *US – FSC (Article 21.5 DSU)*, while domestic practices are not binding means of interpretation,<sup>90</sup> they are informative as to how Members interpreted the SCM Agreement when implementing it into their national laws. Furthermore, as complaints of transnational subsidization have already started being addressed to investigating authorities, these authorities will have to take a stance on this question before any WTO panel. Thus, this section focuses on how some jurisdictions have transposed the relevant provisions of the SCM Agreement into their domestic law and whether they have been faced with issues concerning transnational subsidies.

First, regarding the US, the conflicting purposes described above is what led to the express exclusion of transnational subsidies from the purview of the US anti-subsidy laws. The 1998 amendment

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<sup>87</sup> OECD, *Foreign Direct Investment for Development, Maximising Benefits, Minimising Costs* (2002) <<https://www.oecd.org/daf/inv/investmentfordevelopment/1959815.pdf>>

<sup>88</sup> Vegas, *South-East Asia is Sprouting Chinese Enclaves*, *supra* note 22.

<sup>89</sup> Stewart, *THE GATT URUGUAY ROUND*, *supra* note 7 at 886. See also, ABR, *US – Large Civil Aircraft (2<sup>nd</sup> Complaint)*, *supra* note 53 at para. 1253.

<sup>90</sup> PR, *US – FSC (Art. 21.5 DSU)*, *supra* note 37 at Annex F-3 in para. 110.

incorporated Section 351.527 in the US Code of Federal Regulations, which indicates that funding provided (a) by a government of a country other than the country in which the recipient firm is located; or (b) by an international lending or development institution, would not be countervailable.<sup>91</sup>

Although the policy of the US Department of Commerce (**USDOC**) to not consider assistance from multilateral financial institutions as countervailable started in the 1980s, it was clearly confirmed in the 1993 Court of International Trade (**CIT**) ruling in *North Star Steel Ohio v. the United States*.<sup>92</sup> The CIT explained that the US anti-subsidy law excluded loans granted by the Inter-American Development Bank (**IADB**). The CIT held that the IADB could not be considered as ‘a country under the [SCM] Agreement’,<sup>93</sup> adding that the Government of Argentina had no control over the management of funds that were disbursed by the IADB. The CIT also relied on a USDOC’s determination, where it was decided that the World Bank could not be considered a ‘country under the [SCM] Agreement’.<sup>94</sup> Therefore, it held that the IADB’s loans did not fall within the scope of the US anti-subsidy law.

The background for excluding ‘subsidies by a government other than the government of a country other than the country in which the recipient firm is located’ by the US was probably due to reparations and assistance to development, as mentioned by Professor Gary Horlick.<sup>95</sup> In this regard, in December 1999, the USDOC issued its final affirmative determination in *Steel Plates from India*<sup>96</sup>, where one of the respondents in that investigation was alleged to have received financial support from the World Bank, Kreditanstalt für Wiederaufbau (**KfW**) and Finnish Export Credit (**FEC**). The USDOC excluded the loans from the World Bank and KfW as they were well-known international financing institutions. It also excluded FEC supplier credit loans as FEC was a Finnish government bank. As a result, these ‘transnational loans’ were also excluded.<sup>97</sup> This question has not come up again – the last investigations on this point date back to 1999.

It is worth mentioning that subsidies to international consortia and upstream subsidies provisions are however not excluded from the scope of the US anti-subsidy law. Subsidies to international consortia include subsidies provided by the government of the international consortium but for production in another third country.<sup>98</sup> Upstream subsidies apply to situations of global value chains whereby the supplier of the input is subsidized and passes-through the benefit to an affiliated producer, even if the input supplier is in a foreign jurisdiction.<sup>99</sup>

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<sup>91</sup> 19 Code of Federal Regulation § 351.527 (the US).

<sup>92</sup> *North Star Steel v. United States*, 824 F. Supp. 1074 (the US CIT 1993).

<sup>93</sup> Under Section 701(b) of the Tariff Act of 1930 has been amended from ‘country under this Agreement’ to what a ‘Subsidies Agreement country’ is.

<sup>94</sup> The United States Department of Commerce, Final Affirmative Countervailing Duty Determination, Fuel Ethanol from Brazil, 51 Federal Register 3361 (27 January 1986).

<sup>95</sup> Horlick, *An Annotated Explanation*, *supra* note 80 at 297-299.

<sup>96</sup> The United States Department of Commerce, Final Affirmative Countervailing Duty Determination: Certain Cut-to-Length Carbon-Quality Steel Plate From India [C-533-818], 64 Federal Register 73131 (29 December 1999).

<sup>97</sup> *Id.* at 73141-42.

<sup>98</sup> 19 USC § 1671(d).

<sup>99</sup> 19 USC § 1671(e).

With regard to the way in which the EU has transposed the SCM Agreement into EU law, the EU Anti-subsidy Regulation provides useful information.<sup>100</sup> Under EU law, a transfer of funds by a government of a country which is not the exporting country is not a subsidy. Indeed, Articles 2 and 3 of the Basic Anti-Subsidy Regulation provide that a subsidy exists only if ‘there is a financial contribution by a government in the country of origin or export’. In this regard, the term ‘government’ is previously defined as ‘a government or any public body within the territory of the country of origin or export’. These provisions therefore together indicate that the government or public body as well as the financial contribution needs to be within the territory of the country of origin or export. Interestingly, the Commission when faced by allegations of subsidies to buyers located in the EU explained that ‘subsidies given by a foreign government to entities outside its jurisdiction, such as unrelated importers in the European Union or even the end customer in the European Union are not covered by the instrument insofar as they cannot be attributed to the exporting producer.’<sup>101</sup> The Commission has so far not taken a decision in any of the investigations mentioned at the beginning of this article.

With regard to Canada and Australia, Canada’s anti-subsidy laws do not state anything of value regarding whether transnational subsidies are explicitly excluded from the definition of subsidy as its Special Import Measures Act is worded in a similar fashion to that of the SCM Agreement.<sup>102</sup> Similarly, Australia’s Customs Act 1901 does not contain any reference to transnational subsidies, although it does interestingly address global value chains by considering as subsidies financial contributions that confer a benefit to goods used in the production or manufacture of the goods exported to Australia.<sup>103</sup> The Canadian and Australian investigating authorities have to date not been confronted with an allegation of transnational subsidies.

## 5. Concluding Remarks

As discussed at length in this article, the fact that a government finances a firm which is not under its jurisdiction is not unrealistic anymore. As China increasingly ‘goes global’, allegations of transnational subsidies are likely to be more common. However, the wording of the SCM Agreement prevents such financing from being disciplined thereunder, at least regarding non-prohibited subsidies under Article 3, as it treats the subsidizing Member and the exporting Member as one and the same. This flows from the wording of Article 2.1 of the SCM Agreement, which indicates that the recipient of the subsidy needs to be ‘within the jurisdiction of the granting authority’. It is further confirmed by footnote 63 that defines the recipient of the subsidy for the determination of the amount of subsidization in the ‘serious prejudice’ analysis as ‘a firm in the territory of the subsidizing Member’. Furthermore, the SCM Agreement also gives a series of rights to the exporting Member only.

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<sup>100</sup> Regulation 2016/1037 of the European Parliament and of the Council, OJ 2016 L 176/55.

<sup>101</sup> Commission Implementing Regulation 2017/696, OJ 2017 L 146/9, recital 396.

<sup>102</sup> Section 15, Special Import Measures Act, 1985, Revised Statutes of Canada.

<sup>103</sup> Customs Act, 1901, Compilation No. 158, 3 October 2019, Volume 3, Part XVB—Special Provisions Relating to Anti-Dumping Duties, 269T(1)(2AA) (Australia).

As China relies on financing, which creates global concerns when provided domestically to producers in China, to assist Chinese-owned companies to establish themselves in third countries, transnational subsidies are bound to become increasingly contentious. Although the drafters of the SCM Agreement did not consider this situation, there is now, in the words of Professor Gary Horlick, a need for 'a full analysis of the impact of such cross-border subsidies and consideration of how, or whether, they should be disciplined'.<sup>104</sup>

As the two main limitations to considering transnational subsidies as a 'subsidy' under the SCM Agreement are Article 2.1 and footnote 63, which concern non-prohibited subsidies only, a possible approach would be to interpret the SCM Agreement as covering transnational prohibited subsidies only. As these subsidies are assumed to be the most trade distortive, and by their export-oriented nature, less likely to have development as their primary aim, this approach seems appropriate as it balances the specificities of transnational subsidies with the need to avoid trade distortion.

If states were to consider how to further address transnational subsidies, the objective of disciplining trade-distorting subsidies should be kept in balance with the needs of developing countries to attract foreign companies in order to enhance their economic development. Indeed, countries which are now on the receiving end of the BRI welcome China's involvement as a contributor to their economic growth. As such, the fact that China is now 'going global' while the West is retreating should not blindly alter that conclusion.

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<sup>104</sup> Horlick & Clarke, *Rethinking Subsidy Disciplines*, *supra* note 74 at 695.

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