China's 'Going Global' Policy: Transnational Production 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 becoming heavily scrutinized. 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 that had long been described as 'unrealistic', in which a government subsidizes a firm outside of its territory. When such a firm's products are exported to third countries, could such financing be disciplined under the World Trade Organization 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 a preliminary guidance on how to structure this problem under international trade law.

I. INTRODUCTION

In his recent book, 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'.¹ He further explains that a situation in which 'a government subsidizes a firm which is not under its jurisdiction' should not be considered as it is 'unrealistic'.²

Due to the heavy involvement of the Chinese government throughout its economy, the issue of Chinese subsidies has recently gained considerable attention.³ At the same time, China increasingly 'goes global' through its Belt and Road Initiative (BRI). While

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1 Marc Benitah, *The WTO Law of Subsidies, A Comprehensive Approach* 605 (Wolters Kluwer, 2019) [hereinafter 'Benitah, Subsidies'].

2 Ibid.

3 See generally, Chad Bown and Jennifer Hillman, 'WTO'ing a Resolution to the China Subsidy Problem', 23 (4) *Journal of International Economic Law* 557–578 (2019).

the BRI has started attracting scholarly attention, it still 'remains understudied as a matter of legal analysis'.⁴

As a result of China's expansionist strategy under the BRI, the European Commission (Commission) recently faced what Benitah described as an 'unrealistic' scenario in three anti-subsidy investigations. This article, thus, intends to bridge the issue of Chinese subsidies and the BRI by addressing the question of whether transnational production subsidies—defined for the purpose of this article as the financing by a government (the subsidizing Member) to producers established in a third country (the exporting Member) whose products are exported to other third countries (the importing Members)⁵—can be disciplined under the Subsidies and Countervailing Measures (SCM) Agreement by using China's assistance to Chinese-owned companies located along the BRI as an example.

It first provides a historical background describing the emergence of transnational production subsidies [section I]. Then, this article analyses whether transnational production subsidies fall within the ambit of the SCM Agreement and the remedies available thereunder [section II]. Section III elaborates on whether transnational production subsidies should be disciplined from a policy perspective. Section IV analyses how certain World Trade Organization (WTO) Members have addressed the issue of cross-border subsidies. Finally, section V offers some conclusions.

II. THE EMERGENCE AND INCREASING RELEVANCE OF TRANSNATIONAL PRODUCTION SUBSIDIES

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

4 Heng Wang, 'China's Approach to the Belt and Road Initiative: Scope, Character and Sustainability', 22 (1) *Journal of International Economic Law* 29–55 (2019) [hereinafter 'Wang, China's Approach to the BRI'].

5 We will, thus, not address the question of whether the financing by a government to producers established in a third country whose products cause distortions in this third country's market can be addressed under the SCM Agreement. These subsidies have recently been discussed by the Commission in The European Commission, White Paper on Levelling the Playing Field as Regards Foreign Subsidies, COM(2020) 253 final (17 June 2020), https://ec.europa.eu/competition/international/overview/foreign_subsidies_white_paper.pdf [hereinafter 'Commission, White Paper on Foreign Subsidies'].

A. From national subsidies to transnational subsidies

Following the end of World War II, governments realized that subsidies could have potential trade-distorting effects.⁶ As a result, countries discussed imposing some form of discipline on them in the Havana Charter, and in the General Agreement on Tariffs and Trade (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.⁷

By the 1970s, the use of subsidies had become one of the most frequently used and controversial commercial policies.⁸ 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 at that time called, trade based on 'competitive subsidization' rather than on market forces.⁹ This increase in use of subsidies led to a significant degree of trade distortions, which compelled the GATT signatories to negotiate a Subsidies Code during the Tokyo Round negotiations.¹⁰ Yet, this Subsidies Code still explicitly recognized that subsidies formed an integral part of economic development. It was, therefore, considered that an outright ban on subsidies would forbid developing countries 'to assist their industries'.¹¹

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, which led to even greater subsidization.¹² In 1985, a Preparatory Committee was established for the Uruguay Round to address the issue of subsidies.¹³ In particular, the United States of America 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.¹⁴ The subject of the subsidy negotiations in the Uruguay Round was, thus, focused on curtailing its use

6 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).

7 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: Cambridge University Press 2014) [hereinafter 'Coppens, WTO Disciplines on SCM'].

8 Report of the Director-General of GATT, the Tokyo Round of Multilateral Trade Negotiations, 53 (1979).

9 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'].

10 Preamble, Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariff and Trade ('Subsidies Code') [hereinafter 'Subsidies Code'].

11 Articles 14:1 and 14:2 of the Subsidies Code.

12 Stewart, the GATT Uruguay Round, above n 9 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 (1994). [hereinafter 'Kleinfeld and Kaye, Red Light, Green Light?'].

13 Trade Policies for a Better Future, 'The Leutwiler Report', the GATT and the Uruguay Round 139 (1987).

14 *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*

by States for the purposes of enhancing their domestic industry, so as to avoid subsidy races.¹⁵ Consequently, as explained by the WTO Expert Group on Trade Financing (EGTF) in 2004, the SCM Agreement is 'in general drafted to address situations where a WTO Member is subsidizing the production or sale of its own goods'.¹⁶

However, with unceasing globalization, subsidies have become less domestically focused. It has become common to encounter situations of subsidization that have cross-border 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.¹⁷ Similarly, the rise of large European companies led to subsidies given by one European Union (EU) 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, due to the growth of global value chains, governments may now subsidize a company in their own country who may, by extension, subsequently use this subsidy for production in several other countries.¹⁸

B. 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 cross-border element. As recently discussed by Wang, while there is no clear and widely accepted definition of the BRI due to China's flexible strategy,¹⁹ it is undisputed that one of the main short-term aims of the BRI is to alleviate industrial excess capacity in China by assisting Chinese companies' move abroad.²⁰

While new investment mediums 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.²¹ This financing covers not only infrastructure projects, but also assistance to Chinese companies relocating to third countries. For instance, the Premier of China explained in 2014 that '[w]e encourage competitive Chinese producers of iron and steel, cement and plate, etc. to shift their operation to ASEAN countries

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).

15 Ibid. 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).

16 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'].

17 See for example, Panel Report, *Brazil–Export Financing Programme for Aircraft*, WT/DS46/R (1999) [hereinafter 'PR, Brazil – Aircraft'].

18 See, for example, *Usinor Sacilor v United States*, 991 F. Supp. 665 (the US CIT 1997).

19 Wang, China's Approach to the BRI, above n 4 at 47.

20 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'].

21 Ibid.

to meet the local need of infrastructure development through investment, leasing and loan lending so as to achieve mutual benefit.²² 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.²³

As a result, Chinese state-owned banks have been providing financing in the forms of loans, export guarantees and export insurance to Chinese companies establishing themselves outside China.²⁴ In addition, 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 China's 'preferred mode of economic expansion' as they bring along many Chinese workers with them.²⁵ These industrial parks are meant to become a place for Chinese firms to establish themselves abroad by providing infrastructure and utility services or assisting them in their dealings with local authorities.²⁶

C. Complaints brought to the Commission

These new developments have led to a number of anti-subsidy 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. 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.²⁷ The complainants contended that the producers in Egypt benefit from financial contributions granted '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.'²⁸ Soon after this first complaint, the Commission received another complaint concerning imports of glass fibre products, containing similar allegations, but this time originating solely from Egypt. In October 2019, the Commission received yet another complaint—this time regarding imports

22 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>.

23 See Dirk van der Kley, *China Shifts Polluting Cement to Tajikistan*, Chinadialogue, available at <https://www.chinadialogue.net/article/show/single/en/9174-China-shifts-polluting-cement-to-Tajikistan> (visited 8 August 2016).

24 OECD, China's BRI in the Global Trade, above n 20 at 18–19.

25 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'].

26 HSBC, 'Industrial zones under the BRI', <https://www.business.hsbc.com/belt-and-road/industrial-zones-under-the-bri> (accessed on 26 June 2020).

27 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 (accessed on 26 June 2020).

28 Ibid, at 3.

of hot-rolled stainless steel sheets and coils from China and Indonesia. In the summary of the complaint, the complainants highlighted 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.²⁹ Based on these complaints, the Commission initiated three anti-subsidy investigations.³⁰

The complaints against these forms of assistance 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. 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 EGTF, '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.'³¹ The next section delves into this question.

III. TRANSNATIONAL PRODUCTION SUBSIDIES UNDER THE SCM AGREEMENT

This section assesses whether transnational production subsidies, defined as the subsidization by a government of a producer in a third country whose products are subsequently exported to other third countries, qualify as subsidies under the SCM Agreement and can be addressed thereunder. It is argued that while Article 1 of the SCM Agreement does not impose any clear limitation regarding the location of the recipient of the subsidy, meaning that transnational production subsidies qualify as subsidies (section II.A), the SCM Agreement provides remedies only for prohibited subsidies under Article 3 (section II.B). As Part V of the SCM Agreement provides a series of rights solely to the government of the exporting country, it should be that only multilateral remedies under Part II of the SCM Agreement are available to address these prohibited transnational production subsidies (section II.C).

29 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 (accessed on 26 June 2020).

30 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. Notice of initiation of an Anti-Subsidy Proceeding Concerning Imports of Continuous Filament Glass Fibre Products Originating in Egypt, OJ 2019 C 192/30; 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.

31 Expert Group Meeting on Trade Financing 2004, above n 16 at 5.

A. Transnational production subsidies and the SCM Agreement's definition of subsidy

Article 1.1 of the SCM Agreement provides that a subsidy exists if there is a financial contribution by a government, which confers a benefit. In this section, we address in turn these two elements in the context of transnational production subsidies.

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")'. Horlick recalls that the term 'within the territory' in Article 1 of the SCM Agreement was added following the US negotiators' concerns arising from cases filed in the US in the 1980s, where complainants 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.³² He explains that the negotiators did not intend to open that 'can of worms' as the US was the largest donor of overseas assistance at that time.³³

However, 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', meaning that it does not indicate where the recipient of the financial contribution must be located. This is because the qualifier directly follows the term 'a government or any public body' 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'.³⁴

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 considered a 'subsidy' under Article 1 of the SCM Agreement.³⁵ 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"'.³⁶ 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.³⁷

32 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'].

33 Ibid.

34 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)*'].

35 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)*'].

36 Ibid, 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.

37 PR, *Brazil–Aircraft*, above n 17 at paras 2.1–2.6 and 4.19–4.20.

However, with regard to assistance provided by multilateral financial institutions, 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’ adding that it was important to bear in mind that not all cases of support may involve subsidization that is actionable under the SCM Agreement.³⁸ Similarly, the EGTF explained that aid provided by multilateral development institutions are outside the scope of the SCM Agreement, while also highlighting that no Member had challenged such assistances as a subsidy.³⁹

On this basis, it follows that while Article 1.1(a)(1) of the SCM Agreement may exclude from its scope financial contributions granted by multilateral financial institutions, it does not exclude financial contributions granted to recipients located in a different Member than the subsidizing Member.

2. Recipient of the ‘benefit’

Article 1.1(a)(2) of the SCM Agreement simply indicates that ‘a benefit is thereby conferred’. As such, it does not impose any territorial limitation regarding the location of the recipient of the benefit. This article is, nevertheless, relevant as it is the recipient of the benefit 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”’.⁴⁰ However, the recipient of the benefit needs to be ‘the producer of the exported goods subject to the countervailing investigation’.⁴¹ 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’.⁴² As the same financial contribution can confer a benefit to one or more distinct persons⁴³ and the benefit does not necessarily have to flow directly from the financial contribution,⁴⁴ it is important to assess who is the producer to which the financial contribution grants a benefit. It is this producer that will define the recipient of the subsidy itself.⁴⁵

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.⁴⁶ 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

38 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.

39 Expert Group Meeting on Trade Financing 2004, above n 16 at 5.

40 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’].

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

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

43 ABR, US–Countervailing Measures on Certain EC Products, above n 40 at para 110.

44 Ibid.

45 See Art. 14, SCM Agreement.

46 PR, *Brazil–Aircraft*, above n 17 at paras 4.40–4.48.

Government to foreign aircraft buyers, but that the benefit was to be assessed based on the situation of the Brazilian aircraft producer.⁴⁷ 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.⁴⁸

As a result, while Article 1.1(b) does not limit the location of the recipient of the benefit, the location of the recipient of the benefit as defined thereunder is essential for defining the location of the recipient of the subsidy under the SCM Agreement.⁴⁹

3. Conclusion

It can, therefore, be summarized that financial contributions conferring a benefit by the government of a Member will constitute subsidies under Article 1.1 regardless of the location of the recipient. As such, transnational production subsidies would qualify as ‘subsidies’ under the SCM Agreement.

B. Limitations on the location of the recipient of the subsidy

While transnational production subsidies would constitute subsidies under the SCM Agreement, the availability of multilateral and unilateral remedies under Parts III and V of the SCM Agreement regarding non-prohibited subsidies under Article 1.2 appears to be limited by the location of the subsidy recipient. This is so in virtue of the definition of specificity (section II.B.1), and the guidelines to calculate the amount of subsidization (section II.B.2). Article 25.2 of the SCM Agreement concerning notifications confirms this conclusion.

1. Specificity

Article 1.2 of the SCM Agreement indicates that for multilateral and unilateral remedies to be available, a subsidy needs to be specific in accordance with the provisions of Article 2. Article 2 states that for a subsidy to be ‘specific’, it 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’ for remedies to be available under the SCM Agreement.

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.⁵⁰ The AB also explained that the identification of the jurisdiction of the

47 Ibid, 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)*, above n 35 at Annex F-3, para 110.

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

49 See also on this point, PR, *US–FSC (Art. 21.5 DSU)*, above n 35 at Annex F-3 in para 109.

50 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)*’].

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.⁵¹

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.⁵² '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.'⁵³ However, not all financial contributions are performed by bodies that hold the power to regulate.⁵⁴ This is, for example, the case of the Chinese state-owned banks or private bodies that are entrusted or directed by the government. In such a case, how should 'the jurisdiction of the granting authority' be assessed?

In situations where a body that does not have regulatory powers grants a subsidy, it is necessary to assess which governmental authority is behind that body to determine the granting 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.⁵⁵ Whereas for a public body, this will be the governmental authority that vested this public body with governmental authority.⁵⁶ 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)"'.⁵⁷ 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.⁵⁸ It is, therefore, 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.

51 Ibid, at para 4.167.

52 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 (2nd Complaint)']; PR, *US–Anti-Dumping and Countervailing Duties (China)*, above n 34 at para 7.247.

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

54 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).

55 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).

56 PR, *US–Anti-Dumping and Countervailing Duties (China)*, above n 34 at paras 5.95–5.103.

57 ABR, *US–Anti-Dumping and Countervailing Duties (China)*, above n 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)*, above n 34 at para 7.242.

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

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'.⁵⁹ The traditional understanding of State jurisdiction is, as explained in the *Lotus* case, that it is 'certainly territorial; it cannot be exercised by a State outside its territory'.⁶⁰ Although this understanding may not fully reflect today's reality,⁶¹ the interpretation of the term 'jurisdiction' in Article 2.1 of the SCM Agreement as meaning 'territory' appears to be the most appropriate.

The SCM Agreement's legislative history confirms this interpretation. At a meeting of the Negotiating Group on SCM, '[i]t was proposed to clarify that specificity may exist only within the territory of a signatory'.⁶² 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'.⁶³ 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'.⁶⁴ As a result, both Articles were amended to mention the term 'within the jurisdiction of the granting authority'. The idea that jurisdiction, under WTO law, is mainly territorial is also in line with the views taken by the AB⁶⁵ and by the US in *US-FSC* (Article 21.5 DSU).⁶⁶

59 Oxford English Dictionary, definition of 'jurisdiction' <https://www.oed.com/start?authRejection=true&url=%2Fview%2Fentry%2F102156%3FredirectedFrom%3Djurisdiction#eid>.

60 S.S. 'Lotus', France v Turkey, Judgment, (1927), para 45, PCIJ Series A no 10, ICGJ 248 (PCIJ 1927), 7th September 1927.

61 Alex Mills, 'Rethinking Jurisdiction in International Law', 84 British Yearbook of International Law 187–239 (2014).

62 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).

63 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).

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

65 See, Appellate Body Report, 'United States–Import Prohibition of Certain Shrimp and Shrimp Products', para 133, WT/DSS8/AB/R (1998).

66 Panel Report, *US–FSC* (Article 21.5 DSU), Annex F-3, para 108 where the US explained that '[i]n the case of an alleged subsidy taking the form of a tax measure, it would seem appropriate to interpret the term "jurisdiction" as referring to the taxing jurisdiction of the Member in question'.

Two arguments that the subsidizing Member's jurisdiction could extend to the exporting producer despite it not being located within its territories could be considered.⁶⁷ First, it could be argued that, because of their Chinese shareholding, Chinese companies established abroad fall under the jurisdiction of the Government of China.⁶⁸ However, this argument would appear at odds with *Barcelona Traction*, where the International Court of Justice expressly rejected that the argument 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.⁶⁹ Second, it could be argued that, by virtue of their establishment within special economic zones set up under agreements between the Government of China and the host country, these producers fall within the ambit of China's jurisdiction. This argument would, however, fail unless, if in the specific circumstances of the case, China has effectively acquired the right to make its laws applicable and to enforce them within these zones.⁷⁰

Thus, the concept of 'jurisdiction' in Article 2.1 of the SCM Agreement would appear to remain 'certainly territorial'. Since producers established in third countries are located outside the territory of China, it would follow that these producers are not within the jurisdiction of the Government of China so that subsidies granted to them cannot be specific under Articles 2.1 and 2.2.

As a result, only for transnational production subsidies found to be specific in virtue of Article 2.3, because they constitute prohibited subsidies under Article 3, would the SCM Agreement offer remedies in accordance with Article 1.2. This implies that no

67 We note that the 'effects' doctrine, developed in particular in the context of anti-trust law, hardly seems relevant to the issue of transnational production subsidies as the question is not whether the importing Member can extend its jurisdiction to address these subsidies but whether the subsidized entity is within the jurisdiction of the subsidizing Member.

68 See, Lorand Bartels, 'Does WTO Law Really Not Regulate 'Foreign Subsidies'?', 22 June 2020, <https://www.linklaters.com/en/insights/blogs/tradelinks/2020/june/does-wto-law-really-not-regulate-foreign-subsidies>. For example, in international investment arbitration, the notion of 'control' over a company is sometimes used to assess its nationality based on the nationality of its shareholders or of the person who has the power to nominate a majority of the board of director. See for example, *Franz Sedelmayer v The Russian Federation*, SCC Award, 7 July 1998. Similarly, in the *Kiobel v Shell* judgment, the Court of First Instance of the Hague found that it had jurisdiction over claims brought against Shell's daughter company in Nigeria, See, *Kiobel v Shell*, ECLI: NL: RBDHA: 2019: 4233, District Court of Hague (01 May 2019). In the *Siemens* case, the US applied broad jurisdictional powers to enforce nearly all entities involved in the bribery, including those outside its territory, See, *The US Security and Exchange Commission v Siemens Aktiengesellschaft*, 1:08-cv(-02167 (DDC 15 December 2008).

69 *Barcelona Traction, Light and Power Company, Limited (Belgium v Spain)* Second Phase, International Court of Justice (ICJ), 5 February 1970.

70 *Lotus Case*, above n 60 at para 45. For examples of scenarios where one State was found to have jurisdiction over another State's territory please see, 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); Right of Passage over Indian Territory, Portugal v India, Judgment, Preliminary Objections, [1957] ICJ Rep 125, ICJ 173 (ICJ 1957), 26th November 1957; European Court of Human Rights, *Guide on Article 1 of the European Convention on Human Rights—Obligation to respect human rights—Concepts of 'jurisdiction' and imputability*, 31 December 2019, https://www.echr.coe.int/Documents/Guide_Art_1_ENG.pdf.

remedies are provided under the SCM Agreement for transnational production subsidies to Chinese companies established under the BRI, which are not found to be prohibited subsidies under Article 3.

2. Calculation of the amount of the subsidy to the recipient for actionable subsidies

Footnote 63 to paragraph 2 of Annex IV to the SCM Agreement confirms the conclusion that, with regard to actionable 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 and has now been rendered redundant by Article 31 of the SCM Agreement, 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.⁷¹

Regardless of what interpretation is preferred,⁷² the fact that footnote 63 applied to the determination of serious injury for actionable subsidies confirms that, at least for these subsidies, the recipient of the benefit needs to be located within the territory of the subsidizing Member, confirming that transnational subsidies cannot be subject to multilateral remedies under Part III of the SCM Agreement.

3. Notification

Article 25.2 of the SCM Agreement provides that WTO Members must only notify subsidies which are specific and 'granted or maintained within their territories'. As such, Article 25.2 of the SCM Agreement makes it clear that no cross-border subsidies need to be notified to the WTO. However, the fact that it draws a distinction between specificity and the territory within which the subsidy is granted confirms that there are situations where a subsidy is specific while being granted to an entity outside the subsidizing Member's territory, i.e. transnational production subsidies found to be specific in virtue of Article 2.3 of the SCM Agreement because they constitute prohibited subsidies under Article 3.

4. Conclusion

It follows from this section that while transnational production subsidies can qualify as subsidies under Article 1.1 of the SCM Agreement, Article 1.2 limits the availability of remedies to prohibited transnational production subsidies under Article 3 only.

⁷¹ PR, 'US–FSC (Art. 21.5 DSU)', above n 35 at Annex F-3 in para 107.

⁷² Ibid.

C. Available remedies to address transnational production subsidies

With regard to prohibited subsidies, the SCM Agreement provides for two types of remedies. First, under Part II of the SCM Agreement, a WTO Member can make use of the multilateral remedy option by challenging a prohibited subsidy before the WTO Dispute Settlement Body. Second, under Part V of the SCM Agreement, a WTO Member can impose countervailing duties on imported products which it has found to be subsidized following an investigation. We assess these remedies in turn in the context of transnational production subsidies.

1. Multilateral remedy for transnational production subsidies

Article 4 of the SCM Agreement contains the rules regarding multilateral remedies against prohibited subsidies. These rules appear to allow such multilateral remedies to be taken against the subsidizing Member in case of transnational production subsidies.

Article 4.1 provides that when 'a Member has reason to believe that a prohibited subsidy is being granted or maintained by another Member, such Member may request consultations with such other Member'. Under Article 4 of the SCM Agreement, a Member can, thus, request consultations with the Member that grants or maintains the subsidy and not the exporting Member.⁷³ Article 4.7 then provides that if the challenged measure is found to be a prohibited subsidy, the panel shall recommend that 'the subsidizing Member withdraw the subsidy'. If this is not done, retaliation, in the form of countermeasures, can be allowed against imports from the subsidizing Member under Article 4.10. As such, Article 4 of the SCM Agreement allows the use of multilateral remedies against the subsidizing Member for transnational production subsidies but not towards the exporting Member.

2. Countervailing measures to address transnational production subsidies

While countervailing measures on products originating in the exporting Member's territory could be available, it appears that, under Part V of the SCM Agreement, the exporting Member cannot be perceived separately from the subsidizing Member so that countervailing measures may not be available to address transnational production subsidies.

In particular, 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'.

While nothing would technically prevent the importing Member from extending these procedural rights to the subsidizing Member, the lack of obligation to do so could

73 Benitah, 'Subsidies', above n 1 at 606.

lead to due process violations. For example, in the above-mentioned investigation initiated by the Commission on glass fibre products originating solely from Egypt, the Commission investigated subsidies granted by Chinese public bodies but did not hold consultations with the Government of China prior to the initiation of the investigation.⁷⁴ Furthermore, as the Government of China was not the country of export in this investigation, the Commission 'asked the [Government of Egypt] to provide the information relating to the general legal framework of the banking sector in China as well as concerning financial institutions in China because the [Government of Egypt] is the government concerned by this investigation.'⁷⁵

Such a situation is untenable and contrary to the spirit of the procedural rights provided for under Part V of the SCM Agreement to other WTO Members in anti-subsidy investigations. It leads to the possible absence of fair opportunities for the subsidizing Member to respond to the allegations of subsidizations and to an unsurmountable burden for the exporting Member. In this sense, by granting procedural rights solely to the government of the exporting member in the context of countervailing measures, it seems that in the context of Part V of the SCM Agreement, the subsidizing Member and the exporting Member should be one and the same, which would, thus, exclude transnational production subsidies from the ambit of countervailing measures.

D. Conclusion

It follows from this section that with regard to transnational production subsidies, the SCM Agreement draws two lines. First, as discussed in section II.B, remedies under the SCM Agreement are only available for prohibited subsidies, as Article 2 indicates that a subsidy granted to a benefit recipient outside the territory of the subsidizing Member cannot be found to be specific except if that subsidy is a prohibited subsidy under Article 3. This is further confirmed by footnote 63 of the SCM Agreement and Article 25.2 of the SCM Agreement. Second, as discussed in section II.C, it could be argued that the SCM Agreement only provides for multilateral remedies to address transnational production subsidies, as the provisions of Part V of the SCM Agreement provide procedural rights solely to the exporting Member in anti-subsidy investigations.

IV. DISCIPLINING TRANSNATIONAL PRODUCTION SUBSIDIES OR ALLOWING DEVELOPMENT?

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. Ideally, subsidies that are the most distortive to trade should ideally face a harsher discipline than those that enhance development or address environmental issues.⁷⁶ This section, thus, starts by assessing two contradicting aims of

74 Commission Implementing Regulation 2020/870, OJ 2020 201/10, at 9 [hereinafter 'Regulation 2020/870'].

75 Ibid, at recital 16.

76 Gary Horlick and Peggy Clarke, 'Rethinking Subsidy Disciplines for the Future: Policy Options for Reform,' 20 (3) *Journal of International Economic Law* 673, 695 (2017) [hereinafter 'Horlick and Clarke, Rethinking Subsidies Disciplines'].

the SCM Agreement: curbing trade-distortive subsidies and enhancing development (section III.A). Second, it analyses how this conflicting situation emerges regarding transnational production subsidies (section III.B). Finally, this section tests the conclusion provided in section II.D against this background (section III.C).

A. The SCM Agreement's contradicting aims

The object and purpose of the SCM Agreement reflect the contradicting aims of curbing trade-distortive subsidies and enhancing development. 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,'⁷⁷ even though not every government action or intervention should be considered as a subsidy that may distort trade.⁷⁸ 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 in 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. Article 27.9 of the SCM Agreement⁷⁹ practically addresses this dichotomy as it provides more room for developing Members to grant certain actionable subsidies and allows multilateral remedies against these subsidies only in limited circumstances.⁸⁰

B. The contradicting effects of transnational production subsidies

A parallel can be drawn between the dual purposes of the SCM and the effects of transnational subsidies while these subsidies can greatly benefit the exporting Member's development, they can also have trade-distortive effects. With respect to the BRI, the Economist recently posed the questions 'what exactly is it? Is it mostly aid or trade? Is it a Chinese Marshall Plan?'⁸¹ Through the BRI, China has increasingly assumed the role of being the international investor for developing countries.⁸² However, China's objective for the BRI is to provide assistance to developing countries, on the one hand,

77 PR, 'Brazil–Aircraft', above n 17 at para 7.26.

78 Panel Report, 'United States–Measures Treating Export Restraints as Subsidies', paras 8.62–8.63, WT/DS194/R (2010).

79 Note that Article 27.9 does not apply to China. See, *Report of the Working Party on the Accession of China*, Ministerial Conference—Fourth Session—Doha, 9–13 November 2001, the World Trade Organization, WT/MIN(01)/3, 10 November 2001, para 170.

80 Coppens, 'WTO Disciplines on SCM', above n 7 at 558–563.

81 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>.

82 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.

while expanding China's influence abroad, on the other.⁸³ In this regard, an important aspect of the BRI is that Chinese companies as well as Chinese staff move to third countries.⁸⁴

These differences have created concerns that China has an 'expansionist' agenda, which should be restrained.⁸⁵ 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 mere assistance 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.⁸⁶

Although often criticized, the BRI does bring employment and tax revenue and does increase infrastructure spending to receiving countries.⁸⁷ Thus, considering financing under the BRI as purely a trade distortion that needs to be addressed could be viewed as fear of China's hegemony or a biased Western understanding that disregards developing countries' needs. Thus, while China's cross-border financing is a rising concern, it is important to not bluntly apply the SCM Agreement's disciplines to transnational production 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.

C. Disciplining transnational production subsidies while enabling development: a way forward

In section II.D, we reached the conclusion that the SCM Agreement draws two distinctions when it comes to transnational production subsidies. This section tests the validity of these distinctions in light of the contradicting aims of the SCM Agreement and contradicting effects of transnational production subsidies.

First, the conclusion that only transnational production subsidies qualifying as prohibited subsidies under Article 3 should be disciplined under the SCM Agreement provides a balance for the two conflicting goals of development and trade distortion,

83 David Dollar, 'Is China's Development Finance a Challenge to the International Order?' 13 *Asian Economic Policy Review* 283, 296 (2018).

84 Richard Kozul-Wright and 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>.

85 See generally, Horesh Niv, Kim Hyun Jin, and Mauch Peter, *Superpower, China? Historicizing Beijing's New Narratives of Leadership and Response Thereto* (Singapore: 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>.

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

87 Vegas, 'South-East Asia is Sprouting Chinese Enclaves', above n 25.

discussed above. It leaves space for developing Members to receive transnational production subsidies while allowing importing Members to challenge the use of prohibited export subsidies, which are assumed to be highly trade distortive,⁸⁸ and by their export-oriented nature, are less likely to have development as their primary purpose. This conclusion also mirrors the balance provided for in Article 27.9 of the SCM Agreement, which gives more leeway to developing Members regarding non-prohibited subsidies.

Second, the distinction drawn between the context of countervailing measures and that of multilateral remedies provides an avenue for Members that are affected by transnational production subsidies to raise their concerns with limited effects on the exporting Member. Multilateral remedies provide an appropriate forum to address the trade-distortive effect of transnational production subsidies as it addresses the underlying issue directly, while not negatively impacting Members receiving these subsidies. On the other hand, in the context of countervailing measures, the exporting Member bears the impact of the measures on its own as the countervailing duties are imposed against imports originating therein. Furthermore, countervailing measures may fail to address the underlying issue as the Chinese-owned producers targeted by these measures might simply decide to move shop somewhere else along the BRI leading to the unwanted result that the transnational production subsidies subsist fully while the receiving Member loses the benefit of the foreign investment.

The legal distinctions drawn in section II, thus, fit squarely within the SCM Agreement's aims of disciplining subsidies while allowing developments.

V. DOMESTIC DEVELOPMENTS

As explained by the US in *US–FSC (Article 21.5 DSU)*, while domestic practices are not binding means of interpretation,⁸⁹ they are informative as to how Members interpreted the SCM Agreement when implementing it into their national laws and as to the direction which Members might take to further address the issue of transnational production subsidies, and cross-border subsidies more generally.

The US became aware of this issue early on. Although the policy of the US Department of Commerce (USDOC) to not consider assistance from multilateral financial institutions as countervailable started in the 1980s, the US expressly excluded transnational production subsidies from the purview of the US anti-subsidy laws through the 1998 amendment incorporated in Section 351.527 of the US Code of Federal Regulations. It indicates that funding provided (i) by a government of a country other than the country in which the recipient firm is located or (ii) by an international lending or development institution would not be countervailable.⁹⁰ As explained by Horlick, this was meant to exclude reparations and assistance to development, as the US was the largest aid donor at the time.⁹¹

88 Stewart, 'The GATT Uruguay Round', above n 9 at 886. See also, ABR, 'US–Large Civil Aircraft (2nd Complaint)', above n 52 at para 1253.

89 PR, 'US–FSC (Art. 21.5 DSU)', above n 35 at Annex F-3 in para 110.

90 19 Code of Federal Regulation § 351.527 (the US).

91 Horlick, 'An Annotated Explanation', above n 32 at 297–299.

In December 1999, the USDOC issued its last determination on this issue in *Steel Plates from India*,⁹² 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 FEC supplier credit loans, as FEC was a Finnish government bank. It also excluded the loans from the World Bank and KfW, as they were international financing institutions.⁹³ As a result, these 'transnational loans' were not countervailed.⁹⁴

As discussed in section I, this question recently came under the spotlight in the EU. In this regard, the way in which the EU transposed the SCM Agreement into its domestic law through the Basic Regulation is relevant.⁹⁵ Under EU law, a transfer of funds by a government of a country that is not the exporting country is not a subsidy. Indeed, Articles 2 and 3 of the Basic 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.⁹⁶

Regardless of these limitations, in its recently published regulations imposing countervailing duties on import from Egypt, the Commission decided to countervail transnational production subsidies, arguing that the government of the exporting country, in this case the Government of Egypt, can be 'accountable under the SCM Agreement for having actively sought, acknowledged and adopted' subsidies granted by another government.⁹⁷ The Commission reached this conclusion by interpreting the term 'government' in Article 1.1(a)(1) of the SCM Agreement in light of Article 31(3)(c) of the Vienna Convention on the Law of Treaties (VCLT).⁹⁸ In this regard, the Commission considered that Article 11 of the International Law Commission's Articles on the Responsibility of States for Internationally Wrongful Acts (ILC Articles) constituted 'relevant rules of international law applicable in the relations between the parties'.⁹⁹ Article 11 of the ILC Articles provides that conduct that is not attributable to a State can 'be considered an act of that State under international law if

92 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).

93 On the issue of subsidies granted by international financial institutions under US law, see also, *North Star Steel v United States*, 824 F. Supp. 1074 (the US CIT 1993); The United States Department of Commerce, Final Affirmative Countervailing Duty Determination, Fuel Ethanol from Brazil, 51 Federal Register 3361 (27 January 1986).

94 Ibid, at 73141-73142.

95 Regulation 2016/1037 of the European Parliament and of the Council, OJ 2016 L 176/55.

96 Note India and Brazil's anti-subsidy regulations similarly limit subsidies to financial contributions by the country of export. See, §9, the Customs Tariff Act, 1975 (India) read with Customs Tariff (Identification, Assessment, and Collection of Countervailing Duty on Subsidized Articles and for Determination of Injury) Rules, 1995; Article 4.II, Decree No.1,751, 19 December 1995 (Brazil).

97 Commission Implementing Regulation 2020/77, OJ 2020 189/1, at recital 672 [hereinafter 'Regulation 2020/77'].

98 Ibid, at 685-686; Regulation 2020/870, above n 74 at 73-74.

99 Regulation 2020/77, ibid, at 687-689; Regulation 2020/870, above n 74 at 75-76.

and to the extent that the State acknowledges and adopts the conduct in question as its own.' According to the Commission, as the Government of Egypt welcomed Chinese investments, it made the Chinese preferential measures its own so that financial contributions by Chinese public bodies were attributable to the Government of Egypt.¹⁰⁰ As a result, the Commission concluded that under the Basic Regulation, 'financial contributions in the form of preferential financing from Chinese public bodies to Jushi and Hengshi Egypt can be attributed to the Government of Egypt as the government of the country of origin or export under Article 3.1(a) of the basic Regulation.'¹⁰¹

The Commission's reasoning that Article 11 of the ILC Articles could constitute a relevant rule of international law to interpret the term 'government' in Article 1.1(a)(1) of the SCM Agreement in the sense of Article 31(3)(c) of the VCLT is, however, rather unconvincing. While in *US–Anti-Dumping and Countervailing Duties (China)*, the AB ruled that the ILC Articles constituted a 'relevant' rule of international law, it did so only insofar as Articles 4, 5 and 8 of the ILC Articles reflect the three types of entities whose conduct could be attributed to a government under the SCM Agreement.¹⁰² These entities are organs of the State which are similar to 'a government' under Article 1.1(a)(1) of the SCM Agreement (Article 4), entities exercising elements of governmental authority which are similar to 'a public body' under Article 1.1(a)(1) of the SCM Agreement (Article 5), and persons directed or controlled by a State, which are similar to 'a private body' entrusted or directed by the government under Article 1.1(a)(1)(iv) of the SCM Agreement (Article 8). In other words, the AB did not state in *US–Anti-Dumping and Countervailing Duties (China)* that Article 11 of the ILC Articles constitutes a 'relevant' rule of international law in the sense of Article 31(3)(c) of the VCLT. This is so because Article 1.1(a)(1) of the SCM Agreement does not contain rules with regard to acknowledgment and adoption of a conduct by a State which would be similar to the rules contained in Article 11 of the ILC Articles.

Thus, in light of the recent announcements made by EU Member States and by the Commission regarding their intention to rein in Chinese subsidies,¹⁰³ this decision seems rather political and fits squarely within the current sceptical attitudes towards Chinese foreign investment. In this regard, coincidentally, the Commission, on 17 June 2020, published a White Paper aimed at levelling the playing field in the EU internal market as regards foreign subsidies. In this White Paper, the Commission started exploring the impact of 'foreign subsidies',¹⁰⁴ defined as the financing by a non-EU

100 Regulation 2020/77, *ibid*, at 690–696; Regulation 2020/870, above n 74 at 77–84.

101 Regulation 2020/77, *ibid*, at 697; Regulation 2020/870, above n 74 at 85.

102 Appellate Body Report, 'United States–Definitive Anti-Dumping and Countervailing Duties on Certain Products from China', WT/DS379/AB/R, 25 March 2011, DSR 2011:V, 2869, paras 309–322.

103 Sam Flemming and Javier Espinoza, Brussels Urged to Rein in State-Backed Foreign Rivals, *Financial Times*, 4 December 2019, <https://www.ft.com/content/flf1896-15fa-11ea-9ee4-11f260415385>.

104 While not the focus of this article, we note that the Commission's proposal may not be fully in line with the EU's WTO obligations, in particular with regards to Article 32.1 of the SCM Agreement, the Agreement on Government Procurement, and potentially Articles II, XVI, and XVII of the General Agreement on Trade in Services. For more on this issue see, Lorand Bartels, *WTO Law Implication of the EU's Proposal to Target 'Foreign Subsidies' Given to Companies in Other Countries*, Linklaters, 22 June 2020, <https://www.linklaters.com/en/insights/blogs/tradelinks/2020/june/wto-law-implications-of-the-eus-proposal-to-target-foreign-subsidies-given-to-companies>.

government to a recipient located, or active, in the EU resulting in distortion of competition in the EU market, by noting that 'foreign subsidies appear to have facilitated the acquisition of EU undertakings, influenced other investments decisions or have distorted the market behaviour of their beneficiaries.'¹⁰⁵ Prepared with the US and China in mind,¹⁰⁶ the White Paper notes '[m]any foreign subsidies would be problematic if they were granted by EU Member States and assessed under EU State aid', but that the issue is that 'EU State aid rules however apply only to public support granted by EU Member States. In contrast, subsidies granted by non-EU authorities fall outside EU State aid control.'¹⁰⁷ The Commission, thus, indicated that it will endeavour to design new instruments to address foreign subsidies that distort the internal market and, more specifically, foreign subsidies which facilitate the acquisition of European companies¹⁰⁸ or foreign subsidies in public procurements. It is, however, unclear at this point whether this proposal will be welcomed by a majority of EU Member States, as many EU Member States have joined the BRI and welcome Chinese investment as an engine for their economy.¹⁰⁹ While there are no other similar far-reaching proposals at the moment, many other countries, which, for the most part, have not joined the BRI, have also recently strengthened their investment screening mechanisms to address concerns regarding Chinese investments.¹¹⁰

The issue of cross-border production subsidies also came up in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership in the context of state-owned enterprises.¹¹¹ In particular, Article 17.6(3) addresses the injurious effects of the provision of non-commercial assistance by a party to its state-owned enterprises established in the territory of another party by providing that:

No Party shall cause injury to a domestic industry of another Party through the use of non-commercial assistance that it provides, either directly or indirectly, to any of its state-owned enterprises that is a covered investment in the territory of that other Party in circumstances where:

- 105 Commission, *White Paper on Foreign Subsidies*, above n 5.
- 106 Thibault Larger, Brussels Plans to Counter Chinese and US Subsidies Above €200,000, Politico, 12 June 2020, <https://www.politico.eu/article/brussels-plans-to-counter-chinese-and-us-subsidies-above-e200000/>.
- 107 Commission, *White Paper on Foreign Subsidies*, above n 5.
- 108 See further on this issue, Gary Hufbauer, Thomas Mall and Luca Rubini, *Investment Subsidies for Cross-Border M&A: Trends and Policy Implications*, The United States Council Foundation Occasional Paper No. 2, April 2008, https://www.uscib.org/docs/usc_foundation_investment_subsidies.pdf.
- 109 Europe's 'Sinatra Doctrine' on China, *The Economist*, 11 June 2020, <https://www.economist.com/europe/2020/06/11/europes-sinatra-doctrine-on-china>.
- 110 Jonathan Bonnitcha, 'Investment Wars: Contestation and Confusion in Debate About Investment Liberalization', 22 *Journal of International Economic Law* 629–654 (2019) [hereinafter 'Bonnitcha, Investment Wars']; Countries like India and Australia have also amended/are in the process of amending their investment laws. For example, India has amended its Foreign Direct Investment (FDI) policy to secure itself from Chinese takeovers and acquisitions. See Press Note No. 3(2020 Series), Government of India Ministry of Commerce and Industry, https://dipp.gov.in/sites/default/files/pn3_2020.pdf; For Australia, see, Richard Henderson, Australia adds national security test to foreign investment rules, *Financial Times*, 5 June 2020, <https://www.ft.com/content/f3a1833a-493a-43a8-babb-f2ff3dbc4cc1>.
- 111 Ines Willemyns, 'Disciplines on State-Owned Enterprises in International Economic Law: Are We Moving in the Right Direction?', 19 (3) *Journal of International Economic Law* 657–680 (2016).

(a) the non-commercial assistance is provided with respect to the production and sale of a good by the state-owned enterprise in the territory of the other Party; and

(b) a like good is produced and sold in the territory of the other Party by the domestic industry of that other Party.¹¹²

These developments show that cross-border subsidies are no longer unrealistic. To the contrary, they have become a growing source of concerns as States, and China in particular, increasingly 'globalize' their use of subsidies. While the EU has been the most vocal on this issue so far, other countries are also showing a growing scepticism towards China's outbound investments. As these countries' concerns grow, it is likely that the schism between proponents and opponents to China's expansion will only exacerbate.

VI. CONCLUDING REMARKS

As discussed at length in this article, the fact that a government finances a firm that is not under its jurisdiction is not unrealistic anymore. As China increasingly 'goes global', concerns over cross-border subsidies are growing. Allegations of transnational production subsidies are already becoming more common since 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. Although the drafters of the SCM Agreement did not consider this situation, there is now, in the words of 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.'¹¹³

While transnational production subsidies do meet the definition of subsidy under Article 1.1 of the SCM Agreement, Article 1.2 of the SCM Agreement prevents such financing from being disciplined thereunder regarding non-prohibited subsidies under Article 3. 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' and is further confirmed by Article 25.2 and footnote 63. The SCM Agreement also appears to exclude transnational production subsidies from countervailing measures, as several of the provisions of the SCM Agreement provide procedural rights to the government of the exporting country only in anti-subsidy investigations.

These dichotomies between prohibited and non-prohibited subsidies, and between countervailing measures and multilateral remedies, are in line with the conflicting aims of the SCM Agreement to discipline trade-distortive subsidies, while allowing development. It provides an avenue for Members who consider that their interests are affected by transnational production subsidies to seek redress, while limiting the negative impact that addressing these subsidies might have on the exporting Member.

As transnational production subsidies become more contentious and States reflect on how to tackle this issue, the objective of disciplining trade-distorting subsidies

112 Chapter 17, State-Owned Enterprises and Designated Monopolies, Comprehensive and Progressive Agreement for Trans-Pacific Partnership.

113 Horlick and Clarke, *Rethinking Subsidy Disciplines*, above n 76 at 695.

should be kept in balance with the needs of developing countries to attract foreign companies in order to enhance their economic development. Indeed, countries that 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.