Governments' Interventions into the Real Economy under WTO Law Revisited: New Tendencies of Governmental Support of the Automobile Industry

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The automobile industry has received unprecedented governmental support during the ongoing economic crisis. Rescue packages have been provided to sustain the significant market branch and asserted key driver of growth, export, innovation, and jobs particularly in the EU and the United States and to avoid further downward spirals, which risk affecting the national economies on a wider scale. Since such tendencies can have trade distorting effects, however, the question arises whether the increased governmental interventions are compatible with the World Trade Organization (WTO) legal framework, which arguably enshrines free trade theory in international law. By adopting a legal perspective, this contribution shall address the state's role in global markets and examine the degree of policy space that is conferred to WTO Member States in support of real economy sectors.

1. Introduction

Since September 2008, the global economic crisis that has been lurking on the horizon became blatantly visible, shaking first the financial sector and hence global economy to their very foundations. In response to this worldwide predicament, rescue packages have been tied by national governments, with the objective of supporting different market sectors. In 2007, the financial bailout of the British high-profile Northern Rock bank hit the headlines, only to be followed one year later by the US bailout programmes for major financial institutions such as Citigroup, JP Morgan Chase, Fannie Mae and Freddie Mac, as well as Lehman Brothers before its collapse. Such programmes were still based on the hope that markets would be in a position to provide the essential funds to recapitalize the

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banking sector as a whole on a wider scale.[1] The substantive state interventions implemented as a reaction to the crisis by several national governments and the European Union, not halting before the 'sacred cows' of macroeconomic policies, have shaken the confidence underlying the Western capitalist system, culminating in declarations that capitalism and what is commonly associated with this economic policy is in fact dead.[2] Central banks have adopted measures to enhance liquidity such as interest rate reductions, which were conducted in view of preventing recession and securing the states' financial situation, not least by stimulating the granting of credits to the real economy.[3] Corresponding to their emergency character, several actions have been adopted ad hoc and on a short-term basis. The first responses primarily included recapitalization measures.[4]

As the crisis eventually spread to affect sectors of the real economy, governments were willing to support several industry branches in order to sustain specific markets and prevent rising unemployment levels and reduced consumer demands. Standing out as an illustrative example is the governmental support provided in favour of the automobile industry and its largest companies such as General Motors Corporations (GM) and Chrysler Group LLC (Chrysler) in the United States, as well as its subsidiary Adam Opel GmbH in Europe. Effective state measures adopted included enhancing the businesses' access to financing, for example, by direct provisions of capital in loan contracts. Indeed, the direct government payments to the auto industry have been massive as a glance at the figures provided in the United States illustrates. As an example, GM received approximately USD 50 billion in federal aid; Chrysler was granted USD 6.6 billion in exit financing on top of USD 4 billion it had originally received to avoid bankruptcy and in addition to an immediate loan granted by the Canadian government.[5] The amounts of funding provided to the automobile industry have to be put into perspective in view of the total investments that governments have undertaken as a reaction to the current financial crisis. According to the latest numbers, financial and sectoral support measures have increased the estimate of headline support to 32% of the gross domestic product (GDP) in the G20 countries. The upfront financing provided by the US is estimated to amount to USD 900 billion, that is, 6.3% of GDP.[6] In the EU the support of the banking

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[1] G. Wehinger, 'Lessons from the Financial Market Turmoil: Challenges ahead for the Financial Industry and Policy Makers', *OECD 2008 Financial Market Trends*, <www.oecd.org/dataoecd/47/25/41942918.pdf>, 7 (visited 23 Jun. 2009).

[2] See also Asli Demirgüç-Kunt & Luis Servén, 'Are All the Sacred Cows Dead? Implications of the Financial Crisis for Macro and Financial Policies', World Bank Policy Research Working Paper 4807, January 2009, <http://econ.worldbank.org> (visited 23 Jun. 2009).

[3] Such an approach has been illustrated by the interest policies adopted by both the Federal Reserve System and the ECB.

[4] See Wehinger, above n. 1, at 7 et seq. with an overview over some major policy responses, which included, *inter alia*, financial support to subprime lenders, rescues of individual major financial institutions by government purchases of assets, swaps of government securities, debt issuance, the implementation of general and coordinated government guarantees and insurances, and capital injections for the financial industry.

[5] See 'General Motors Corporation Overview', *The New York Times*, 16 Jun. 2009, <http://topics.nytimes.com/top/news/business/companies/general_motors_corporation/index.html?scp=1-spot&sq=GM%20&st=cse> (visited 23 Jun. 2009); 'Chrysler LLC Overview', *The New York Times*, updated 10 Jun. 2009, <http://topics.nytimes.com/top/news/business/companies/chrysler_llc/index.html?scp=1-spot&sq=chrysler&st=cse> (visited 23 Jun. 2009).

[6] See IMF Update on Fiscal Stimulus and Financial Sector Measures, 26 Apr. 2009, <http://imf.org/external/np/fad/2009/042609.pdf> (visited 23 Jun. 2009).

sector alone has amounted to about 13% of GDP with approved funds worth another 31% of GDP. Indeed, the public debt-to-GDP ratio in the EU is estimated to have surpassed the 60% mark in 2008 and to reach 79.4% until 2010.[7]

Besides direct payments, the support of national economies was addressed, *inter alia*, by reducing taxation, in order to raise consumer demand, and support export opportunities.[8] Furthermore, states acquired preferred shares, thus establishing public-private partnerships according to which shareholders' equity is increased.[9] Indeed, according to GM's restructuring plan and agreement with both the US Treasury and the Canadian and Ontario governments, the 'new GM' will be owned by the US Treasury holding 60%, the Canadian and Ontario governments holding 12.5%, besides the new Voluntary Employee Beneficiary Association (New VEBA) holding 17.5% and 10% held by unsecured bondholders.[10]

In the globalized world of today, such developments seem to reverse the shift in perception that became apparent at the latest with the Fall of the Berlin Wall in 1989, challenging the role of the states as the primary players and subjects of the international legal framework according to traditional Westphalian notions of international law and factually attributing private players, including individual and legal persons, a substantial position. Such developments were based, *inter alia*, on the still prevailing economic theory on free trade and growth, according to which market interventions by national governments are generally deemed problematic. From this point of view, governmental interferences risk to throw the open self-regulated economies off balance and to falsify the equilibrium implied by the free market, thus resulting in inefficiencies and global trade distortions. On the basis of such perceptions, the Final Declaration of the Summit on Financial Markets and the World Economy held on 15 November 2008 by the Group of Twenty (G20) emphasized that the reforms and actions taken to mitigate the global financial crisis had to be 'grounded in a commitment to free market principles' and generally rejected protectionism despite the present times of uncertainty.[11] This statement

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[7] European Commission, Public Finances in EMU 2009, European Economy, 10th edn, Brussels, 5 Jun. 2009, <http://ec.europa.eu/economy_finance/publications/publication_summary15289_en.htm> (visited 23 Jun. 2009).

[8] See, e.g., the Declaration on a Concerted European Action Plan of the Euro Area Countries, adopted at the Summit of the Euro Area Countries on 12 Oct. 2008, <www.eu2008.fr> (visited 23 Jun. 2009).

[9] As an example, the US government has not shied away from purchasing preferred stock from Citigroup, thus becoming holder and owner of about one-third of the bank's equity. Additionally, in Germany, the expropriation of private stockholders has been discussed in general (see 'Gesetz zur weiteren Stabilisierung des Finanzmarktes (FMStErgG)' [BGBL I S 725], which entered into force on 9 Apr. 2009. See also James Wilson and Bertrand Benoit, 'Germany ready to move on radical HRE plan', *Financial Times*, 19 Mar. 2009, <www.ft.com/cms/s/0/4d22f5f8-1426-11de-9e32-0000779fd2ac.html?nclick_check=1> (visited 23 Jun. 2009); 'The state and the economy: Germany, how to restart the engine? ', *The Economist*, 14 Mar. 2009, 28–29). Furthermore, the United Kingdom's (UK) Banking Act, which entered into force on 21 Feb. 2009, is noteworthy in this respect. Indeed, the third stabilization option under the UK Banking Act goes as far as allowing the bank in question to be taken into temporary public ownership (see ss 11–13 of the UK Banking Act 2009, <www.opsi.gov.uk/acts/acts2009a> (visited 23 Jun. 2009). See also 'Bank bail-outs: Quids pro quo', *The Economist*, 20 Nov. 2008, <www.economist.com/finance/displaystory.cfm?story_id=12651361> (visited 23 Jun. 2009).

[10] Existing GM shareholders have, however, objected to this plan according to which they are expected to be wiped out. See 'GM Announces Agreement with US Treasury and Canadian Governments Providing Fast Track to Competitive Future for New GM', 1 Jun. 2009, <www.gm.com/restructuring> (visited 23 Jun. 2009); The Associated Press 'New Objections May Delay GM Exit from Bankruptcy', *The New York Times,* 19 Jun. 2009, <www.nytimes.com/2009/06/20/business/20auto.html> (visited 23 Jun. 2009).

[11] G20 Declaration of the Summit on Financial Markets and the World Economy, Washington, DC, 15 Nov. 2008, <www.g8.utoronto.ca/g20/2008-leaders-declaration-081115.html> (visited 23 Jun. 2009).

has been repeated over and over again ever since, not least by the Director-General of the World Trade Organization (WTO), Pascal Lamy, the Central Bank Governors and the Group of Seven (G7) Finance Ministers, as well as the high-level participants at the G20 conference in early 2009.[12]

The increased governmental interventions into the economy of private enterprises have raised questions on whether governments are assuming a new role in private industry and the globalized markets. Is there a shift taking place, away from the free market towards increased regulation and governmental ownership? Are we facing an era of a new economic system or a new form of capitalism as the speech of France's President, Nicolas Sarkozy, held in Toulon on 25 September 2008 would suggest?[13] And how are such new developments compatible with the current regulatory frameworks in place?

It is difficult to obtain verified, precise, and reliable information due to the fact that WTO Members seem rather reluctant to provide official information to the WTO Secretariat in the current turbulent situation.[14] The objective of this contribution is therefore not the presentation of an actual case study and its solution. Rather a more abstract approach is chosen. In light of the recent developments, the subject matter on governments' market participation in the real economy shall be revisited by casting light on the states' support of the automobile industry, which has become a conspicuous example of governmental intervention particularly in Europe and the United States.[15] By adopting a legal perspective, the paper addresses the state's role in global markets from a WTO law point of view, which is arguably addressed as the fundamental legal framework that enshrines the worldwide economic system and its underlying values. Thereby, two aspects of the trade-dimension of governmental support of the auto industry can be distinguished: First, the state measures improve the credit of auto companies relative to their foreign competitors and strengthen the ties between the firms and the government. Second, the emerging 'Car Czars' could use this power in sales competition against foreign brand rivals.[16] The contribution shall tackle the differentiation between legal and illegal state interventions in support of the automobile industry under WTO law and

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[12] See WTO News Item of 9 Feb. 2009, <www.wto.org/english/news_e/news09_e/tpr_09feb09_e.htm> (visited 23 Jun. 2009); Statement of G7 Finance Ministers and Central Bank Governors, Rome, 14 Feb. 2009, <www.g7finance.tesoro.it> (visited 23 Jun. 2009); see the G20 Leaders' Statement, The Global Plan for Recovery and Reform, London, 2 Apr. 2009, at paras 22–24; see also the wording of the G20 countries' different communiqués, all available at <www.g20.org/pub_communiques.aspx> (visited 23 Jun. 2009).

[13] Or in the words of Nicolas Sarkozy: 'L'autorégulation pour régler tous les problèmes, c'est fini. Le laissez-faire, c'est fini. Le marché qui a toujours raison, c'est fini' (Original speech is available at <www.sarkozynicolas.com/nicolas-sarkozy-discours-de-toulon-texte-integral> (visited 23 Jun. 2009)).

[14] See unofficial first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, 23 Jan. 2009, WTO Doc. JOB(09)/2, at para. 6, kindly made available by the WTO Information and External Relations Division.

[15] An assessment of the European interventions into the banking sector in the context of the current financial crisis is provided in a further contribution (Rolf H. Weber & Seraina Grünewald, 'Finanzkrise und Wirtschaftspolitik: Herausforderungen für das Europäische Wettbewerbsrecht', *Zeitschrift für Europarecht (EuZ)* 3 (2009): 58–67. For an economic analysis of the purpose and design of the GATT/WTO framework, see, e.g., Kyle Bagwell & Robert W. Staiger, *The Economics of the World Trading System* (Cambridge, Massachusetts/London: MIT Press, 2002).

[16] Claire Brunel & Gary Clyde Hufbauer, 'Money for the Auto Industry: Consistent with WTO Rules?', Petersen Institute for International Economics, February 2009, <www.petersoninstitute.org> (visited 23 Jun. 2009).

shall assess the scope of discretion that states possess in the free market in compatibility with the international trade legal framework.

2. The Free Trade Theory Revisited: States' Role to Play in Free Markets

Although different theoretical economic models have been developed, the current economic system is based on economic growth and free market theories, that is, a liberal system whose origins can be traced back to the eighteenth century and the oeuvres written by Adam Smith[17] and David Ricardo[18] in particular. Based on the assumption that international free trade generates global gains, which supply the trading partners with benefits in the short term and growth and development in the longer run,[19] the theory of comparative advantage frames the backbone of the international trading system until today.[20] This school of thought started to materialize during the Second World War with the prominent Atlantic Charter[21] that laid the cornerstones for the establishment of a multilateral trading system, which was formally initiated by the conference of the political leaders of the time in Bretton Woods, USA, in 1944.[22] Furthermore, the establishment of a market-based economy was particularly illustrated by the creation of the single integrated internal market of the EU[23] which significantly expanded to encompass the Central-Eastern European countries since the fall of the Iron Curtain.

Although the free market theory has been strongly criticized and cannot be deemed undisputed, since the 1990s, its prevailing position has been endorsed by a vast normative framework established *inter alia* under the auspices of the United Nations[24] and institutionalized not least by international organizations such as the WTO, as well as the International Monetary Fund (IMF) and the World Bank having, among others, laid the foundations for the liberalization of international capital and monetary transactions; while the IMF

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[17] Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (edited by Edwin Cannan), (Chicago: University of Chicago Press, 1976). For an overview on Smith's theory, see Karl Pribram, *Geschichte des ökonomischen Denkens*, Band I (Frankfurt am Main: Suhrkamp, 1992), 243–261.

[18] David Ricardo, *The Principles of Political Economy and Taxation* (London: John Murray, 1817) (reprinted in London/Rutland 1973), 81.

[19] H. Jessen, 'Trade and Development Law', in *Sustainable Development in World Trade Law*, eds Markus W. Gehring & Marie-Claire Cordonier Segger (The Hague: Kluwer Law International, 2005) 77–101, at 98.

[20] For an overview on international trade history, see Michael J. Trebilcock & Robert Howse, *The Regulation of International Trade*, 3rd edn (London/New York: Routledge 2005), at 1–26; see also Alan O. Sykes, 'Comparative Advantage and the Normative Economics in International Trade Policy', *Journal of International Economic Law* 1 (1998): 49–82 at 60–61. See also Pribram, above n. 17, at 280–318.

[21] Official Statement on Meeting Between the President and Prime Minister Churchill (14 Aug. 1941), in *The Public Papers and Addresses of Franklin D. Roosevelt*, ed. Samuel I. Rosenman (New York: Random House, 1950), 314.

[22] Generally, on the proceedings of the conference, see Proceedings and Documents of the United Nations Monetary and Financial Conference, Bretton Woods, New Hampshire, 1–22 Jul. 1944 (1948); for an overview, see Rolf H. Weber & Douglas W. Arner, 'Toward a New Design for International Financial Regulation', *University of Pennsylvania Journal of International Law* 29 (2007): 393–400.

[23] See Completing the Internal Market: White Paper from the Commission to the European Council, 28–29 Jun. 1985, COM(85) 310.

[24] See the commitment to a liberal multilateral trading system reiterated in several documents adopted under the auspices of the United Nations, e.g., at para. 13 of the United Nations Millennium Declaration, 18 Sep. 2000, UN Doc A/RES/55/2 stating: 'We are committed to an open, equitable, rule-based, predictable and nondiscriminatory multilateral trading and financial system.' This was reiterated, e.g., in paras 27–32 of the 2005 World Summit Outcome, 24 Oct. 2005, UN Doc A/RES/60/1.

specifically works to foster global monetary cooperation, secure financial stability, and facilitate international trade, the World Bank is mandated to advance the vision of an inclusive and sustainable globalization by providing low-interest loans, interest-free credits and grants to developing countries for a wide array of purposes. Not surprisingly, the Preamble to the Agreement establishing the WTO sets ambitious goals with the following words:

> *Recognizing* that their relations in the field of trade and economic endeavour should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development,
>
> *Recognizing* further that there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development,
>
> *Being desirous of* contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade relations,
>
> *Resolved*, therefore, to develop an integrated, more viable and durable multilateral trading system encompassing the General Agreement on Tariffs and Trade, the results of past trade liberalization efforts, and all of the results of the Uruguay Round of Multilateral Trade Negotiations,
>
> *Determined* to preserve the basic principles and to further the objectives underlying this multilateral trading system,
>
> Agree as follows: (...)[25]

As preambular clauses, such objectives do not provide for directly enforceable legal obligations. Nevertheless, they constitute specific values and guidelines underlying the global multilateral trading system under the auspices of the WTO legal framework.

With the establishment of the legal branch of international economic law under the auspices of its regulatory bodies, nation states have placed themselves into the double-edged position of eventually curtailing their own influence on the global markets by opting for a multilateral trading system. It has become a rather common claim that the nation states are rapidly losing their influence on the international sphere as a consequence of globalization, or in other words, due to increasing networks of governance regimes, particularly restraining national political autonomy. This development is – not coincidentally – also referred to as a time of 'post-nationalism'.[26]

As already implied by the notion of free markets, the theoretical framework places special emphasis on the economic mechanisms that are to be held free from market interventions. According to Smith, the welfare of society is thus coupled with the consistent multiplication of production in what he referred to as a 'progressive state'. A progressive state, he argued, is based on a '*laissez faire*' policy, ensuring a broad scope for the development of an open economy by granting its individuals a free hand regarding the

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[25] Marrakesh Agreement establishing the World Trade Organization, 15 Apr. 1994, WTO Doc LT/UR/A/2, emphasis adopted from the original document.

[26] Markus Krajewski, *National Regulation and Trade Liberalization in Services* (The Hague: Kluwer Law International, 2003), xvii.

setting of market parameters such as price formation and the functioning of competitive structures. In his terms, a 'well-governed society' supports and protects ideal market conditions. The role of the state, according to Smith, was thus seen in the promotion of reduced trade barriers, the furtherance of economic and innovative potential, and the supply with trade supportive communication and transport systems.[27] Apart from such tasks, the states were also entrusted with a prominent role in terms of a sociopolitical responsibility for public welfare. For example, they were deemed responsible for tackling and countervailing potentially damaging tendencies in the free market in support of the common good. Indeed, already Smith approved the regulation of the banking sector and the control of the rate of interest.[28] A certain degree of mistrust characterized his skeptical approach towards the 'bankers', namely, the 'few individuals, which might endanger the security of the whole society',[29] a position of eye-catching topicality in light of the current financial and economic deteriorations.

Such a limited role of the state and a general focus on market mechanisms have been readopted by various modern economic theories and have culminated in trends often associated with the Chicago school of economics, also referred to as the so-called freshwater school of economics. According to this school of thought, regulatory market interventions generally result in less efficient processes than would be achieved by the absolute realization of free markets in terms of the invisible hand. Governments' participation is thus cut back as far as possible to avoid inefficient outcomes, based on the trust in 'natural' market processes. The Chicago School has been subject to severe criticism, particularly by the so-called saltwater schools of economics based in the coastal universities of the United States, such as notably Harvard, MIT, and Berkeley, splitting the US continent in two.[30]

Without having to go as far as such 'market fundamentalist' views, governments' interventions into free markets have been deemed particularly problematic based on several lines of reasoning. Apart from the general comprehension that interventions into the free market lead to inefficiencies, there is the argument that, in addition to their lack of expertise, government officials will often face conflicts of interest originating from their dependency of an electorate or political base and reward supporters, respectively. Moreover, the ultimate consequence of private mismanagement in a market economy, namely, bankruptcy, is generally no imminent worst case scenario for the public sector. To the contrary, bureaucrats will often lack incentives that reward efficient resource allocation.[31]

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[27] Smith, above n. 17, Book I, Ch. I, at 15.

[28] Smith, above n. 17, Book II, Ch. II, 342–345, 350; *Id.*, Book II, Ch. IV, 379–380; on education in the context of employment, see particularly Book I, Ch. X, 111 et seq.

[29] Smith, above n. 17, Book II, Ch. II, at 344–345.

[30] On the Chicago school of economics, see, e.g., Milton Friedman, *On Economics: Selected papers* (Chicago: University of Chicago Press, 2007); Milton Friedman, *Capitalism and Freedom* (Chicago: University of Chicago Press, 2002); George J. Stigler, *Chicago studies in political economy* (Chicago/London: University of Chicago Press, 1988). More critical assessments on the Chicago school of economics are provided, e.g., by Sherryl Kasper, *The revival of laissez-faire in American macroeconomic theory* (Cheltenham, UK/Northampton, MA: Edward Elgar Publishing Ltd, 2003); Robert H. Nelson, *Economics as religion: from Samuelson to Chicago and beyond* (Pennsylvania: Pennsylvania State University Press, 2001).

[31] Demirgüç-Kunt/Servén, above n. 2, at 12–16.

In the specific context of the economic crisis, two particular points of criticism were uttered. On the one hand, it was considered as problematic that governments occupy the role otherwise played by the market, by determining who the 'winners' and the 'loosers' should be. Instead of letting market mechanisms 'reward' and 'punish' the market participants, the governments have assumed responsibility for deciding in an administrative process, which market players they are willing to support and which ones they prefer to drop. On the other hand and especially in light of the bailout programmes of the United States, such an interference was interpreted as an unfair transfer of wealth from ordinary tax payers to the rich world, that is, the upper percentage of influential managers and CEOs, whereas the rest of the world was burdened by the losses resulting from the economic crisis.[32]

Despite the objections against the government as a market participant, however, the expectation that public welfare can be achieved without governmental intervention, based on a sole self-regulative economy, has proved to be rather illusionary. This is particularly reflected in the development of different conceptions and theories on competition and antitrust enforcement,[33] as well as with regard to the roles of policies and institutions regarding economic development.[34] Indeed, government ownership of banks as a consequence of banking crises has been a rather popular instrument throughout history. Furthermore, the state as a 'temporary caretaker' of financial institutions and the central bank function as a lender of last resort has not always been equally disputed.[35] Such a wider comprehension of states' responsibilities can also be seen as an underlying pillar of an emerging legal theory on international trade regulation and a rationale for the establishment of a legal framework under the auspices of the WTO, not as a restriction of markets and of freedom according to deregulation and neoliberal philosophies, but moreover as a foundation of markets and freedoms.[36]

3. Framing the Challenges

3.1. Governmental market participation's conceptualization in general

State action must – in accordance with the rule of law – be endorsed by legislative acts. Regulations, as the name suggests, generally refer to the elaboration of 'rules' in promotion

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[32] See, e.g., Eric Dash, 'Few Stand to Gain on this Bailout, Many Lose', *The New York Times*, 7 Sep. 2008, <www.nytimes.com/2008/09/08/business/08scorecard.html?scp=10&sq=winners%20loosers%20credit%20crisis&st=cse> (visited 23 Jun. 2009).

[33] Rolf H. Weber, *Wirtschaftsregulierung in wettbewerbspolitischen Ausnahmebereichen* (Baden-Baden: Nomos Verlagsgesellschaft, 1986), 49–62; see also Krajewski, above n. 26, at 18–20. See Robert Pitotsky (ed), *How the Chicago School Overshot the Mark* (Oxford: OUP, 2008).

[34] Douglas W. Arner, *Financial Stability, Economic Growth and the Role of Law* (Cambridge/New York et al.: CUP, 2007), 14–22.

[35] Demirgüç-Kunt & Servén, above n. 2, at 12 et seq. with further references.

[36] Thomas Cottier & Matthias Oesch, *International Trade Regulation, Law and Policy in the WTO, the European Union and Switzerland, Cases Materials and Comments* (Berne/London: Staempfli Publishers Ltd./Cameron May Ltd. London, 2005), 44 et seq. on a legal theory on international trade law, which seems to lack tradition in legal theory, however, being undisputedly of paramount importance for the functioning of international trade; see also Thomas Cottier, 'Challenges Ahead in International Economic Law', *Journal of International Economic Law* 1–13 (2009), 5. See also *Id.*, 4–6, 10–11 on the role of law.

of specific economic and social objectives.[37] Two approaches can be distinguished that address the economic rationale for legitimate governmental regulation differently:[38] (1) According to traditional perceptions on state regulation the states' responsibilities and administrative competences, respectively, are often limited to the particular public policy objectives that cannot be effectively and efficiently achieved by market mechanisms. In cases of 'market failures'[39] or if the markets' unregulated outcomes are not deemed 'just' or 'fair' in society,[40] state intervention and regulation are seen as a viable and necessary option in the public interest; thereby, economic and non-economic policy goals can be distinguished. The state is thus called upon in terms of the subsidiarity principle, that is, after the market-based approach has failed to achieve the intended outcomes.[41] (2) A more recent school of thought based on public choice theory perceives regulatory policies as serving primarily private interests and is referred to as private interest regulation.[42] A particular focus branch is the regulatory capture theory. This doctrine is critical on the perception of regulatory interventions as being strictly motivated by the objective of protecting public goods and refers to situations in which governments regulate in favour of the commercial or special interests dominating the industry or sector that is regulated, as opposed to public interests.[43]

In accordance with public interest regulation approaches, but historically pre-existing, is the comprehension that, in times of crisis, states undisputedly have to be in the position to adopt the measures necessary to secure their functioning. Such a perception of a state's role can be traced back to the very origins of the nation state and is indeed conceived as a core understanding of state duties and responsibilities. It is generally well grounded in states' constitutions and can also be referred to as a general principle of law recognized in international law according to Article 38(1)(c) of the Statute of the International Court of Justice.[44] On the international stage, this principle of 'necessity' has been adhered to as a justification for states' non-compliance with other international state obligations. According to Article 25 of the International Law Commission's (ILC) Articles on State Responsibility,[45] necessity can prevent the wrongfulness of an act not

[37] For a conceptualization of 'regulation', see Krajewski, above n. 26, at 1 et seq.; Weber, above n. 33, at 27–38.

[38] Krajewski, above n. 26, at 12 et seq.

[39] According to economic theory, several major areas of market failures can be distinguished, namely, (1) natural monopolies, (2) externalities, (3) information deficiencies, (4) ruinous competition, (5) natural scarcity of goods. For an overview on market failures, see Krajewski, above n. 26, at 13–16; Weber, above n. 33, at 98–126.

[40] For example, it is generally acknowledged that private business practices resulting in monopolies, cartels, or other joint practices such as the abuse of dominant market positions may limit competition and consequently cause welfare losses, which are deemed as unjust and unfair in society. Non-economic goals such as ethical values of distributional or social justice objectives are more controversial. See Krajewski, above n. 26, at 18–20.

[41] For a thorough overview on normative public choice, see Dennis C. Mueller, *Public Choice III*, 3rd edn (Cambridge: CUP, 2003), 563–656.

[42] Krajewski, above n. 26, at 20–21.

[43] See, *inter alia*, George J. Stigler, 'The theory of economic regulation', *Bell Journal of Economics and Management Science* 2 (1971): 3–21.

[44] Statute of the International Court of Justice, 26 Jun. 1945, <www.icj-cij.org/documents/index.php?p1=4&p2=2&p3=0> (visited 23 Jun. 2009). Art. 38(1)(c) reads: 'The Court, whose function is to decide in accordance with international law such disputes as are submitted to it shall apply: …c. the general principles of law recognized by civilized nations'.

[45] ILC Draft Articles on the Responsibility of States for Internationally Wrongful Acts, 3 Aug. 2001, adopted at the ILC's fifty-third session and reported to the General Assembly in November 2001, 53 UN GAOR Supp. (No. 10), 43, UN Doc A/56/10.

in conformity with an international obligation, if the state's act chosen instead '(a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and (b) does not seriously impair an essential interest of the State or States towards which the obligation exists or of the international community as a whole.'

Necessity has been invoked to preclude the wrongfulness of acts contrary to a very wide panoply of state obligations in order to protect various interests ranging from the protection of the environment and the securing of the safety of a civilian population to the preservation of the very existence of a state and its people in times of public emergency.[46] The latter argumentation was adopted not only in light of armed conflicts and terrorist attacks[47] but also as a legal line of argument for the justification of a state not clearing its debts due to financial difficulties.[48] However, stringent conditions have to be met in order to reach compliance with Article 25 of the ILC Articles on State Responsibility. *Inter alia*, essential interests must be threatened by grave and imminent peril and the chosen course of action taken by the state must be the 'only way' available to safeguard that interest.

Despite general concerns accompanying governmental action in free markets, it is thus recognized that states have a role to play in a liberal economic system. This is all the more the case with regard to economic crises, in which it amounts to a state responsibility to secure its own standing with a sound economic system, ultimately ensuring its own survival and, not least, economic stability, as well as employment and real income for its citizens. As a consequence, the question cannot be framed as *whether* states are in the position to adopt regulatory measures but moreover on the qualitative aspects of the *characteristics* and the *extent* of legally justified state interventions.

Generally speaking, governments possess a broad scope of discretion regarding the adoption of state measures. Recommendations are given, for example, by the IMF in favour of a stable international economic system or the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC).[49] Both the IBRD and the IFC in particular have set up a Bank Recapitalization Fund, which will not only provide financing but also provide for advisory services for the strengthening of the private sector development and the improvement of the economic and financial

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[46] For an overview, see the examples to Art. 25 of the ILC Draft Articles on the Responsibility of States for Internationally Wrongful Acts with commentaries, printed in the Yearbook of the International Law Commission, 2001, Vol. II, Part Two. See also International Court of Justice (ICJ), Gabcíkovo-Nagymaros Project (Hungary v. Slovakia), Judgment of 25 Sep. 1997, Separate Opinion of Vice-President Weeramantry, ICJ Reports 1997, at 88.

[47] On the legal responses to violent crises and emergencies see Oren Gross & Fionnuala Ní Aoláin, *Law in Times of Crisis, Emergency Powers in Theory and Practice* (Cambridge/New York et al.: CUP, 2006).

[48] See Russian Indemnity Case, 11 Nov. 1912, United Nations Reports of International Arbitral Awards (UNRIAA), Vol. XI (1912), 421–447, at 442–443, in which the Ottoman Empire drew on 'force majeure' to justify its delay in paying its dept to the Russian Government. The case is also outlined in the commentaries to the ILC Draft Articles on the Responsibility of States for Internationally Wrongful Acts, above, n. 46, at 81. See among others, Christian Tietje, 'Die Argentinien-Krise aus rechtlicher Sicht: Staatsanleihen und Staateninsolvenz', *Beiträge zum Transnationalen Wirtschaftsrecht*, Heft 37, February 2005, <www.telc.uni-halle.de/Heft37.pdf> (visited 23 Jun. 2009), at 16 et seq.

[49] R.H. Weber & V. Menoud, *The Information Society and the Digital Divide, Legal Strategies to Finance Global Access* (Zurich/Basel/Geneva: Schulthess Juristische Medien AG, 2008), at 70–107.

performance;[50] such general recommendations and advice, however, do not amount to much more in terms of legal bindingness than policy guidelines.[51] In the case of a granted IMF loan, the IMF Member country's discretion may, however, be limited by an arrangement with the IMF according to which the state in question is held to implement specific policies and measures to resolve its balance of payments problem. Other than that, on an international level, monetary policy is exercised on the basis of broad discretion and within international networks of central banks and monetary authorities, with the Basle Accords as examples of such soft law regulations. Similarly, in the aftermath of the current crisis, a set of principles was established by the G20, which may provide for some non-binding guidance.[52] However, hardly any stringent law is in place, albeit the fact that financial services form a dense and specialized area of domestic law.[53]

On a regional level, the EU legal framework stipulates the obligation of states to inform the European Commission about the potential domestic implementation of state aid measures in order to uphold the principles of fair competition and a single market; the Commission's approval is a necessary prerequisite for the state aid's compatibility with the internal market. Furthermore, Article 87 paragraph 3(b) EU[54] provides for an exception to the general prohibition of possibly anticompetitive state aids in the case of 'serious disturbance of the economy of a Member State'. The general importance of acting in a coordinated manner within the framework of the single market and the Economic and Monetary Union (EMU) has been repeatedly emphasized on a European level and thus obliges the Member States to collaborate and coordinate their action.[55] In view of the current credit crunch, the European Commission has provided a detailed overview on Member States' manifold opportunities for public support under existing state aid rules and has set out additional state aid measures, which Member States may grant temporarily in order to remedy difficulties regarding access to finance and to promote investment pursuing environmental objectives in particular with the adoption of the Temporary Community Framework for State aid measures to support access to finance in the current financial and economic crisis, which applies until 31 December 2010.[56]

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[50] See <www.ifc.org/ifcext/about.nsf/Content/BE76390D8137548385257515007AE5D6?> Open Document and the IFC Bank Recapitalization Fund Fact Sheet, <www.ifc.org/ifcext/about.nsf/AttachmentsByTitle/IssueBrief_BRF/$FILE/IssueBrief_BRF.pdf> (visited 23 Jun. 2009).

[51] Obviously, if the country is in severe financial trouble and thus poses a potential threat for the international financial system, which the IMF is responsible to help protect, the IMF lending program may be initiated, which entails several further state duties.

[52] G20 Declaration of the Summit on Financial Markets and the World Economy, above n. 11.

[53] Cottier, above n. 36, at 4–5.

[54] Treaty on European Union (Nice consolidated version), 24 Dec. 2002, OJ 2002 C 325/5.

[55] See the outcome of the Informal Meeting of Heads of State or Government held in Brussels on 1 Mar. 2009, press release, <www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/misc/106390.pdf> (visited 23 Jun. 2009).

[56] Communication from the Commission – Temporary Community Framework for State Aid Measures to Support Access to Finance in the Current Financial and Economic Crisis, 7 Apr. 2009, OJ 2009 C 83/1 (consolidated version). On state aid measures in support of environmental protection under EU competition law, see R.H. Weber & M. Grosz, 'Erleichterte Beihilfengewährung zugunsten des Umweltschutzes – Legitimation von Wettbewerbsverzerrungen in Krisensituationen', in *Schweizerisches Jahrbuch für Europarecht 2008/2009*, eds Astrid Epiney & Nina Gammenthaler (Zürich/Basel/Genf: Schulthess Verlag, 2009), at 365–384.

Beyond such requirements, no harmonized regulatory and legally binding framework is in place to steer governmental intervention into a specific direction in times of economic crises. However, the different other obligations a state assumes, which may amount to legally binding regulatory schemes, limit the governments' latitude in choosing policy responses. The following study shall focus on the obligations states incur under the WTO legal framework.

3.2. Governmental support of the real economy during the current economic crisis

In response to the current financial deteriorations, unprecedented financial rescue packages were tied up and continue to be laced in order to prevent the collapse of the national economies involved and reduce the risk of contagion throughout the international financial system.

The most significant actions taken in terms of governmental support of specific industry branches concern the automobile industry, where several countries including Argentina, Australia, Canada, China, France, Germany, Japan, Russia, and the United States have introduced support packages in favour of domestic automakers, which included federal loans and loan guarantees, incentives for car buyers and car dealers, as well as support for research and improved innovation.[57]

Due to the fact that the automobile industry produces goods that may be deemed as nice to have as opposed to a necessity for living, it could be questioned whether the governmental support implemented for the benefit of the automobile industry corresponds to the sector's importance for the economy.[58] However, the focus on such a rather 'luxurious' market branch shall not obscure the fact that linked to the automobile industry are numerous jobs and thus various individuals that are affected by the deteriorations of the current economic crisis. Reasons for the specific focus on the recovery of the automobile industry as a specific branch of the real economy are manifold. The governments' firm and generous reactions have been ascribed to the fact that at present, the automobile sectors are significant economic engines of nations, not least due to their key driver function for growth, exports, innovation, and jobs and their strong linkage to a wide variety of other sectors.[59] The automotive industry has increasingly come under pressure in the context of the dramatic rise of energy prices in summer 2008, in addition to the general financial meltdown; in the US in particular, this sector lived on

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[57] See the third Report to the TPRB from the Director-General on the Financial and Economic Crisis and Trade-Related Developments, 14 Jul. 2009, WTO Doc. WT/TPR/OV/W/2, at paras 72, 75, 94, and the first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 37; International Centre for Trade and Sustainable Development (ICTSD), 'WTO Report Finds "Limited Evidence" of Protectionism amidst Economic Crisis', *Bridges Weekly Trade News Digest* 13, no. 3 (28 Jan. 2009). See also 'The state and the economy: Germany', *The Economist*, above n. 9 at 28–29; 'The state and the Economy: France, Back in the driving seat', *The Economist*, 14 Mar. 2009, 29. See also Brunel & Hufbauer, above n. 16, at 4–6.

[58] OECD Report, Economic Policy Reforms, Going for Growth 2009, <www.oecd.org> (visited 23 Jun. 2009), at 20 and at 24–25.

[59] Communication from the Commission – Responding to the crisis in the European automotive industry, 25 Feb. 2009, COM(2009) 104 final, 1.

credits similar to the housing markets, a fact that is often employed to explain the quite simultaneous downturn of these markets.[60]

While different measures are applied on a local level, the extent of the support provided nationally within the United States, on the one hand, and regionally within the European Union, on the other hand, stands out in particular. To be precise, the response adopted by the European Union as a supranational organization in this regard should be distinguished from nation states' governmental interventions.[61] However, not least due to its economic authority, the EU's reactions were frequently compared to the arrangements adopted on the other side of the Atlantic Ocean.

In response to the crisis, the United States enacted the Emergency Economic Stabilization Act (EESA) in October 2008, authorizing the United States Secretary of Treasury to spend up to USD 700 billion to purchase distressed assets, such as mortgage-backed securities, and make capital injections into the banking sector. The purpose of this bail-out of the United States financial system includes the restoration of liquidity and the stabilization of this sector of the United States according to a comprehensive, harmonized strategy.[62] In February 2009, the Obama Administration set further priorities to address the economic crisis 'on all fronts' with the Financial Stability Plan.[63]

In light of the mounting pressure on the automobile manufacturers GM and Chrysler in particular, the President Bush administration had already agreed to an emergency bail-out by providing USD 13.4 billion from the Troubled Assests Relief Program (TARP) funds that US Congress had authorized to rescue the financial industry.[64] Under the Obama administration and based on the EESA, further investment programs were enacted, which also targeted the real economy in the field of the automobile industry in particular with the Automotive Industry Financing Program.[65] While the Task Force on the Auto Industry continued to review the restructuring plans submitted by both GM and Chrysler, the US Department of Treasury announced an 'Auto Supplier Support Program' in March 2009 with the aim of providing up to USD 5 billion to stabilize the auto industry.[66] It had become apparent that both GM's and Chrysler's survival were in substantial doubts without additional government loans.

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[60] See the third Report on the Financial and Economic Crisis and Trade-Related Developments, above n. 57, at paras 23 et seq. See also Brunel & Hufbauer, *supra* n. 16, at 1, 2, 5; Eric Dash, 'Auto Industry Feels the Pain of Tight Credit', *The New York Times*, 27 May 2008, <www.nytimes.com/2008/05/27/business/27auto.htm> (visited 23 Jun. 2009); Larry Webster, 'GM in Crisis – 5 Reasons Why America's Largest Car Company Teeters on the Edge', *Popular Mechanics*, 18 Nov. 2008, <www.popularmechanics.com/automotive/new_cars/4292379.html> (visited 23 Jun. 2009).

[61] For a brief outline, see EU Press Release, State aid: Overview of national measures adopted as a response to the financial and economic crisis, Brussels, 16 Feb. 2009, MEMO/09/67.

[62] Section 2 of the Emergency Economic Stabilization Act, H.R. 1424, <http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:h1424enr.txt.pdf> (visited 23 Jun. 2009).

[63] See the Fact Sheet on the Financial Stability Plan, 10 Feb. 2009; see also the Treasury White Paper on the Capital Assistance Program and its Role in the Financial Stability Plan. Both documents and further information is available at <www.treas.gov/initiatives/eesa> and <www.financialstability.gov> (both visited 23 Jun. 2009).

[64] See 'General Motors Corporation Overview', above n. 5. See also Brunel & Hufbauer, *supra* n. 16, at 2 with further references.

[65] They also include the Capital Purchase Program, the Targeted Investment Program, the Program adopted for the backup of the American International Group Inc. (AIG) on fixed rate cumulative perpetual preferred stock offering. The agreements are available at <www.ustreas.gov/initiatives/eesa/agreements/index.shtml> (visited 23 Jun. 2009).

[66] See the Fact Sheet on the Auto Supplier Support Program, <www.treas.gov/press/releases/docs/supplier_support_program_3_18.pdf> (visited 23 Jun. 2009).

Chrysler indeed combined its restructuring plan with an increase of its original loan request on USD 3 billion by another USD 2 billion. While US President Obama rejected the plan, the Canadian government announced an immediate loan of USD 201 million. Nevertheless, after the government's task force had concluded that Chrysler could no longer survive as a stand-alone company, Chrysler was ordered to complete a partnership with the Italian automaker Fiat or face bankruptcy. The US government was strongly involved in the restructuring process of the enterprise, which included talks with the Chrysler debt holders.[67] After negotiations with smaller creditors failed, however, the corporation was forced to seek Chapter 11 protection. On 10 June 2009, Chrysler emerged from bankruptcy after having restructured its enterprise and particularly having transferred assets to Fiat. The US government provided Chrysler with USD 6.6 billion in exit financing.[68]

In addition to the financial support given to the automobile industry, including the backing of warranties for providing consumers with enough confidence to continue purchasing cars, the government's interventions in policy making and governance decisions stand out as significant interferences in the private industry's matters. They became striking when Mr. Wagoner, GM's chairman and chief executive, was forced to resign as a condition for the US government to continue extending their financial aid. Furthermore, the state's auto task force had concluded in its report that GM was apt to make considerable progress in developing new energy-efficient cars and was given sixty days to present a cost-cutting plan for their restructuring while being kept afloat by the government during that time. However, after having received more than USD 20 billion from the state but estimating that tens of billions more were necessary to save the corporation, and in light of the fact that bondholders were reluctant to swap the loans for stock in the reorganized company, GM declared bankruptcy under Chapter 11 on 1 June 2009.[69] GM's restructuring plan now envisages that the majority of the company's assets are transferred to a 'new GM', with the US government set to emerge as the biggest shareholder with a 60% stake, and the governments of Canada and Ontario adopting another 12.5%, thus leading to a process of GM's nationalization. Furthermore, 17.5% will be adopted by the United Auto Workers (UAW), whereas

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[67] Bill Vlasic & Sheryl Gay Stolberg, 'US Expected to Give More Money to Automakers', *The New York Times*, 28 Mar. 2009, <www.nytimes.com/2009/03/28/business/economy/28auto.html> (visited 23 Jun. 2009); Sheryl Gay Stolberg & Bill Vlasic, 'US Lays Down Terms for Auto Bailout', *The New York Times*, 30 Mar. 2009, <www.nytimes.com/2009/03/30/business/30auto.html> (visited 23 Jun. 2009); Z. Kouwe & M. Maynard, 'Chrysler Bankruptcy Looms as Deal on Debt Falters', *The New York Times*, 30 Apr. 2009, <www.nytimes.com/2009/04/30/business/30auto.html?hp=&pagewanted=print> (visited 23 Jun. 2009).

[68] See 'Chrysler LLC Overview', above n. 5; see also M.J. De la Merced & M. Maynard, 'Fiat Deal with Chrysler Seals Swift 42-Day Overhaul', *The New York Times*, 11 Jun. 2009, <www.nytimes.com/2009/06/11/business/global/11chrysler.html> (visited 23 Jun. 2009); see also J. Rutenberg & Bill Vlasic, 'Chrysler Files to Seek Bankruptcy Protection', *The New York Times*, 30 Apr. 2009, <www.nytimes.com/2009/05/01/business/01auto.html> (visited 23 Jun. 2009).

[69] See 'General Motors Corporation Overview', above n. 5; see also B. Simon, N. Bullock, & J. Macintosh, 'GM in race to depart Chapter 11 protection', *The Financial Times*, 2 Jun. 2009, <www.ft.com/cms/s/0/829647ac-4f96-11de-a692-00144feabdc0.html> (visited 23 Jun. 2009); Tom Braithwaite, Julie MacIntosh, Bernard Simon, & John Reed, 'GM to file for Chapter 11 protection', *The Financial Times*, 31 May 2009, <www.ft.com/cms/s/0/e75423ac-4df8-11de-a0a1-00144-feabdc0.html> (visited 23 Jun. 2009).

the remaining 10% will be distributed among the bond holders of the original GM enterprise.[70]

The collapse of the big players in the automobile industry and GM in particular consequently had a severe impact on the companies' subsidiaries in Europe, such as Opel and Saab Automobile AB. With help from the German government and from the Canadian-Austrian car parts maker Magna International, Opel's bankruptcy was finally prevented. The German government brokered a deal for an alliance between the Russian bank Sberbank and GM, each acquiring 35% stake of Opel, as well as Magna International, which will own 20%. Ten percent will be held by Opel employees.[71] By contrast, the Swedish government was not prepared to provide Saab with governmental aid. Saab will now be sold to a consortium headed by a Swedish maker of luxury sports cars, provided that USD 600 million of financing will be granted from the European Investment Bank (EIB) and guaranteed by the Swedish government.[72]

On a supranational level, the European Union also endeavours to take coordinated, joint action to ensure a more effective and credible response, enabling the EU to act as a whole in a united manner. For this purpose, the measures adopted are held to comply with the regulatory framework in place on state aid according to the EC Treaty and as outlined above. In light of the current economic turmoil, the Commission has adopted a temporary framework applicable to state aid measures.[73] Additionally, budget policies must be in line with the rule-based framework provided with the Stability and Growth Pact (SGP), which coordinates national fiscal policies in the EMU in order to ensure sound public finances.[74] In November 2008, the European Commission adopted a European Economic Recovery Plan with two major pillars based on the fundamental principles of solidarity and social justice. The fist pillar envisages boosting demand and stimulating confidence, by injecting purchasing power into the economy. The Commission proposed an agreement to adopt an immediate budgetary impulse of EUR 200 billion. The second pillar relies on direct short-term actions to reinforce Europe's competitiveness in the long term, by adopting a comprehensive programme to direct action to 'smart' investment.

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[70] See, *inter alia*, Bernard Simon, 'GM plans comeback a month early', *The Financial Times,* 19 Jun. 2009, <www.ft.com/cms/s/0/ba24d158-5c6a-11de-aea3-00144feabdc0.html?> (visited 23 Jun. 2009); see also GM Press Release, above n. 10.

[71] N.D. Schwartz, 'With Sale, GM Europe Avoids Fray', *The New York Times,* 1 Jun. 2009, <www.nytimes.com/2009/06/02/business/global/02euro.html> (visited 23 Jun. 2009); J. Dempsey & D. Jolly, 'Effects of Opel Deal Ripple Across Europe', *The New York Times*, 31 May 2009, <www.nytimes.com/2009/06/01/business/global/01opel.html> (visited 23 Jun. 2009).

[72] See 'Saab Automobile AB Overview', *The New York Times*, updated 16 Jun. 2009, <http://topics.nytimes.com/top/news/business/companies/saab_automobile_ab/index.html?scp=1-spot&sq=saab&st=cse> (visited 23 Jun. 2009); see also S. Lyall, 'Sweden Says No To Saving Saab', *The New York Times*, 23 Mar. 2009, <www.nytimes.com/2009/03/23/world/europe/23saab.html> (visited 23 Jun. 2009).

[73] See Communication from the Commission – The Application of State Aid Rules to Measures Taken in Relation to Financial Institutions in the Context of the Current Global Financial Crisis, 25 Oct. 2008, OJ 2008 C 270/8; Communication from the Commission – The Recapitalization of Financial Institutions in the Current Financial Crisis: Limitation of Aid to the Minimum Necessary and Safeguards Against Undue Distortions of Competition, 15 Jan. 2009, OJ 2009 C 10/2; Communication from the Commission – Temporary Community Framework for State Aid Measures, above n. 56.

[74] For more information on the SGP, see <http://ec.europa.eu/economy_finance/sg_pact_fiscal_policy/index_en.htm?cs_mid=570> (visited 23 Jun. 2009).

Furthermore the 'Actions for Recovery', suggested by the European Commission[75] envisages to put the right objectives into place.[76] A specific policy response to the crisis in the automotive sector was provided in late February 2009 by the European Commission and endorsed by the Council of the European Union one month later; it adheres to the CARS 21 Mid-term review High Level Conference conclusions, as adopted on 29 October 2008, as the guiding forces for the future decision-making processes.[77] Furthermore, it allocates primary responsibility for dealing with the crisis to the industry but additionally aims at creating framework conditions and targeted and temporary public sector support at both the supranational and the domestic Member State's level, by restoring the availability of financing and restoring liquidity, boosting demand for new vehicles, and accelerating fleet renewal, safeguarding skills, and employment, as well as minimizing social costs, and ensuring open markets and fair competition.[78] The Council thereby invited the Commission (1) to assess any possible new legislative initiatives in line with the principles by avoiding unnecessary administrative burdens on businesses, (2) to present by the end of 2009 a roadmap of envisaged (legislative and non-legislative) initiatives with a significant impact on the automotive industry approximately over the next three years, and (3) to continue the dialogue with the industry and the relevant stakeholders as a follow-up of the CARS 21 initiative on a regular basis.[79] Furthermore, the European Commission's initiatives to tackle the impact that the current economic deteriorations have on employment deserve mentioning in this context.[80]

On a more institutional level, the European Central Bank (ECB) has reduced interest rates and has adopted further measures in accordance with the national central banks in order to ensure the liquidity of the financial system and to maintain confidence and stability.[81] In the same context, the EIB decided to mobilize EUR 30 billion to support European small and medium sized-enterprises (SMEs) and endorse infrastructure projects.[82] In March 2009, the directors of the EIB authorized an amount of

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[75] Communication from the Commission – A European Economic Recovery Plan, 26 Nov. 2008, COM(2008) 800 final. See also Communication from the Commission for the Spring European Council – Driving European Recovery, 4 Mar. 2009, COM(2009), 114 final. See furthermore the Recovery Plan's precedent documents, namely, Presidency Conclusions, Brussels, 15 and 16 Oct. 2008, 14368/08; Communication from the Commission – From Financial Crisis to Recovery: A European Framework for Action, 29 Oct. 2008, COM(2008) 706 final.

[76] Regarding the specific automotive industry, the main objectives set out by the Recovery plan are (1) the support of demand in order to assist with remedying the effects of the credit squeeze, (2) the facilitation of the adjustment by cushioning the costs associated with restructuring in particular for workers and their upgraded training, (3) the encouragement of the modernization of the plants to ensure sustainable competitiveness of the industry at a world wide level, and (4) the assistance of the industry to implement the radical technological change required by the climate change challenge.

[77] The CARS 21 Mid-Term Review High Level Conference, Conclusions and Report can be found at <http://ec.europa.eu/enterprise/automotive/pagesbackground/competitiveness/cars21_mtr_report.pdf> (visited 23 Jun. 2009).

[78] See Communication from the Commission – Responding to the crisis in the European automotive industry, above n. 59. See also Council of the European Union, Council Conclusions on the automotive industry 6227/09, adopted on 10 Mar. 2009, <http://ec.europa.eu/enterprise/automotive/pagesbackground/competitiveness/7367_09_en.pdf> (visited 23 Jun. 2009).

[79] See Council Conclusions on the automotive industry, above n. 78, at para. 10.

[80] Communication from the Commission – A Shared Commitment for Employment, 3 Jun. 2009, COM(2009) 257 final.

[81] See, e.g., European Central Bank, Monthly Bulletin January 2009, <www.ecb.int/pub/pdf/mobu/mb200901en.pdf> (visited 23 Jun. 2009).

[82] See EIB communication, EIB launches new loans for SMEs, 3 Oct. 2008, <www.eib.org/about/news/eib-loan-for-smes.htm> (visited 23 Jun. 2009).

EUR 3 billion in loans to Europe's auto industry with further financial support expected.[83] The European Bank for Reconstruction and Development (EBRD) tied a further finance package that allows for an increase in the EBRD's annual business volume of about 20% in 2009, which amounts to approximately EUR 7 billion. This cash injection also aims at supporting the banking sector where the EBRD invests and at ensuring the flowing of finance, specifically to SMEs. In late February 2009, the heads of the World Bank Group, the EBRD, and the EIB communicated their willingness to cooperate in a joint programme to lend up to EUR 24.5 billion, in order to find solutions to tackle the economic crisis particularly in Central and Eastern Europe.[84]

Most notably, both the US and the EU have linked their financial support of the auto manufacturing sector to innovative ecological projects in the fields of energy efficiency, green technology, etc.[85] The original loan and security agreement between the US and GM prior to bankruptcy held that the financing secured by the state was to be implemented for developing business with minimal adverse effects on the environment and to enhance the capacity of the enterprise and its subsidiaries to develop and produce energy-efficient advanced technology vehicles; GM was particularly required to submit to the US Treasury Department a detailed restructuring plan, demonstrating long-term viability and including information on the transformation of its business to include fuel-efficient cars and trucks and to enhance environmentally safe automobile production.[86] The 'new GM' now aims at increasing its investment and leadership in fuel economy and advanced propulsion technologies, thereby reaffirming its commitment to improve the fuel efficiency of its vehicles. Regarding Chrysler, the task force instructed the forming of a partnership with Fiat as a condition for receiving another round of government aid. Fiat had signalled its readiness to transfer new technologies for the production of new energy-efficient cars and motors in the United States.[87]

In order to enhance its environmental performance, the EU has temporarily authorized its Member States to ease access to finance for companies through subsidized guarantees and subsidies for investments going beyond EU environmental standards.[88] Furthermore, the EU has adopted a framework for the particular sector of the automotive

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[83] See EIB communication, EIB Directors approve EUR 3 billion in loans to Europe's auto industry, 12 Mar. 2009, <www.eib.org> (visited 23 Jun. 2009). See also Brunel & Hufbauer, above n. 16, at 5–6.

[84] Communiqué by the European Bank for Reconstruction and Development, the European Investment Bank Group and the World Bank Group, Joint IFI Action Plan In Support of Banking Systems and Lending to the Real Economy in Central and Eastern Europe, 26 Feb. 2009, <www.ebrd.com/new/pressrel/2009/com.pdf> (visited 23 Jun. 2009).

[85] Furthermore, US Congress considered the establishment of a National Incentive Program for Voluntary Retirement of Fuel-Inefficient Vehicles, also referred to as 'Cash for Clunkers'. See Brunel & Hufbauer, above n. 16, at 3–4.

[86] See the Loan and Security Agreement between the US Treasury and GM, 31 Dec. 2008 and the 2009–2014 Restructuring Plan, 17 Feb. 2009. Both documents are available at <www.ustreas.gov/initiatives/eesa> (visited 23 Jun. 2009).

[87] See 'Chrysler LLC Overview', above n. 5; B. Vlasic and S. Gay Stolberg, 'US Expected to Give More Money to Automakers', *The New York Times*, 28 Mar. 2009, <www.nytimes.com/2009/03/28/business/economy/28auto.html> (visited 23 Jun. 2009); Sheryl Gay Stolberg and Bill Vlasic, 'US Lays Down Terms for Auto Bailout', *The New York Times*, 30 Mar. 2009, <www.nytimes.com/2009/03/30/business/30auto.html> (visited 23 Jun. 2009)>; Z. Kouwe and M. Maynard, 'Chrysler Bankruptcy Looms as Deal on Debt Falters', *The New York Times*, 30 Apr. 2009, <www.nytimes.com/2009/04/30/business/30auto.html?hp=&pagewanted=print> (visited 23 Jun. 2009). See also Brunel & Hufbauer, above n. 16 at 2–3.

[88] See Communication from the Commission – Temporary Community Framework for State Aid Measures, above n. 56, at para. 4.5.

industry, with the objective of not only offering 'a cushion for the automotive industry in a time of intense pressure, but a springboard for the future.'[89]

4. State Interventions Under WTO Law

4.1. Preliminary remarks

State interventions implicate different problematic aspects. Besides entailing possible distortions of competition in the specific sectors, which are subject to Article 87 of the EC Treaty on a regional level, such attempts also threaten to amount to trade barriers, which are addressed by the states' international trade law obligations under the WTO legal framework.

International trade regulation essentially addresses the conflicts of interests emerging from discussions on domestic or regional trade policy instruments with regard to their potentially restrictive effects on market access for goods and services. The question on the tolerable and legal extent of governmental interventions in free markets is thus a very essential element of international trade law.

Nevertheless, the WTO's institutional and regulatory framework does not address the role of the states in general. Its wording merely implies that it aims at the reduction of tariffs and other protectionist trade barriers, as well as at the elimination of discriminatory treatment in international relations. Thereby the WTO Preamble refers to the 'basic principles… [and] objectives underlying this multilateral trading system'. Although the WTO Agreement does not expressly name such 'basic principles', their content can be deduced from the different trade agreements adopted under the WTO umbrella framework. Generally speaking, the concept of non-discrimination may be interpreted as founding one of the most generic characteristics of trade liberalization. Its two forms, namely, 'most-favoured-nation treatment', on the one hand, and 'national treatment', on the other hand, lie at the core of the multilateral trading system.[90] International trade regulation has the overall objective of reducing differential treatment and securing equal conditions of competition for foreign and domestic comparable products. The fundamental distinction between protectionism and legitimate policy goals thus becomes decisive. Contemporary economists generally agree on the economic theory fundamental, namely, that free trade increases overall welfare. Protectionism, on the contrary, is deemed as reducing such global gains and is consequently perceived as an unwanted characteristic of any trade regulation.[91] WTO law consequently aims at reducing trade barriers that are implemented to protect domestic industries from foreign competition. Such measures may amount to

[89] See Communication from the Commission – Responding to the crisis in the European automotive industry, above n. 59, at 2–3. See also Press Release of the Council of the European Union, Council Conclusions on the Contribution of the Council (Environment) to the Spring European Council (19 and 20 Mar. 2009), 28th Environment Council Meeting, Brussels, 2 Mar. 2009.

[90] Krajewski, above n. 26, at 6; on these principles in more depth, see, *inter alia*, John H. Jackson, *The World Trading System, Law and Policy of International Economic Relations*, 2nd edn (Cambridge, Massachusetts/London: MIT Press, 1997), 157–173, 213–228; Trebilcock/Howse, above n. 20, at 49–111; Cottier/Oesch, above n. 36, at 346–427; Peter Van den Bossche, *The Law and Policy of the World Trade Organization, Text, Cases and Materials* (Cambridge, New York et al.: CUP, 2005), 307–372.

[91] Cottier/Oesch, above n. 36, at 54–55.

explicit import barriers such as quantitative import restrictions or tariffs or may come to light in more subtle forms, such as domestic regulations, which, in effect, discriminate against imports although, at first glance, they seem to treat all competitors alike.

The different measures adopted by the states in the aftermath of the economic downturn, particularly in order to backup the real economy branches, such as the automobile industry, as well as the construction, steel, and airline sectors, risk to result in potentially protectionist measures, with the aim of shielding domestic producers from the economic crisis: Besides the packages adopted in favour of the stimulation of the domestic economies outlined above, tariffs have been raised considerably.[92] Furthermore, various potential non-tariff trade barriers have been introduced, ranging from governmental support for certain market branches to anti-dumping measures, which have been induced against specific imports,[93] the imposition of increased licensing requirements,[94] direct trade restrictions, as well as the limitation of open ports and airports for particular imports.[95] Although some countries have established measures to facilitate trade in these difficult times,[96] the concerns of illegality of such potentially protectionist subsidizing measures prevail; a corresponding communication has already been uttered by the European Commission chief José Manuel Barroso regarding the United States aids for its struggling auto industry.[97] Against this background, world leaders have repeatedly warned about protectionism as a path to global economic ruin that should be categorically avoided, to prevent the worsening of the economic situation for all and the decline of prospects for an early recovery.[98]

It is in view of such considerations that the subsequent outline shall examine the measures adopted for the support of the automobile industry, after drawing an outline on the applicable international rules on subsidization. The focus is set on this particular market branch as an example of a supported real economy sector, for the purpose of shedding light on the states' admissible margin of discretion under the WTO/General

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[92] For example, the MERCOSUR Member States have agreed in November 2008 to raise their common external tariff by 5% points on average on specific items, such as wine, dairy products, textiles, leather goods, and wood furniture (see first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 26).

[93] Such an estimation, however, is based on informal reports; official WTO data are not yet available (see first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 35).

[94] Argentina has imposed such requirements on products considered as sensitive, such as auto parts, textiles, TV, toys, shoes, and leather goods (first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 29).

[95] Indonesia as an example has limited its open ports to five, which may serve as entry points for imports (first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 28). For an overview on the trade-related policy measures adopted, see Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at paras 25–37.

[96] For example, India adopted import restrictions on steel products in November 2008 (first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 25), China has increased VAT rebates on its exports, Argentina has cut its export taxes on wheat and corn by five percentage points, etc. (first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 33).

[97] See, e.g., 'EU might complain to WTO over US car plan – Barroso', *Thompson Reuters*, 14 Nov. 2008, <www.reuters.com/article/marketsNews/idUSLE47953820081114> (visited 23 Jun. 2009). 'Barroso Theatens to Take US to WTO over the Car Rescue Plan,' *Europolitics*, 14 Nov. 2008.

[98] See WTO Director-General Pascal Lamy's speech held on 9 Feb. 2009 in presenting his report on recent trade developments associated with the financial crisis, stating: 'we must remain extremely vigilant' (<www.wto.org> (visited 23 Jun. 2009)). See also first Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14; G20 Declaration of the Summit on Financial Markets and the World Economy, above n. 11.

Agreement on Tariffs and Trade (GATT) rules on subsidization when interfering in the market's equilibrium.

4.2. Applicable rules on subsidization

Rules addressing generally 'unfair' trade situations, which are now distinguished into 'dumping' and 'subsidization' under international trade law, can be traced back much further than the nineteenth century. National provisions addressing subsidies seem to have evolved tightly linked to the regulations on countervailing duties, that is, the importing countries' response to subsidized imports. The development of multilateral international rules applicable to subsidies and countervailing measures (SCM) in particular, however, began with the establishment of the GATT and was further developed under this legal framework's auspices.[99]

4.2.1. *Subsidies' Regulation in the GATT*

Subsidies are addressed in the GATT 1994 in Article VI, in Article III:8(b), and in Article XVI, without however providing for a definition on subsidies.[100] These provisions' main features already existed under the GATT 1947.

(1) Article VI of GATT 1994 allows anti-dumping and countervailing duties to be levied by members on imports that are deemed to cause harm to domestic industries due to their subsidization by a foreign government.[101] Section 3 of Article VI delineates the term 'countervailing duty' as meaning 'a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export of any merchandize'. Such duties may be imposed on

[99] On the applicable rules' evolution, see Jackson, above n. 90, at 285–293. See also Carsten Grave, *Der Begriff der Subvention im WTO-Übereinkommen über Subventionen und Ausgleichsmassnahmen* (Berlin: Duncker & Humblot, 2002), 66–81 and 82–100; Trebilcock/Howse, above n. 20, at 262 et seq.; Cottier/Oesch, above n. 36, at 990 et seq.; Van den Bossche, above n. 90, at 551 et seq.; Marc Benitah, *The Law of Subsidies under the GATT/WTO System* (London: Kluwer Law International, 2001); G.E. Luengo Hernández de Madrid, *Regulation of Subsidies and State Aids in WTO and EC Law, Conflicts in International Law*, Alphen aan den Rijn: Kluwer Law International, 2006), 33 et seq.; Gary Horlick & Peggy A. Clarke, 'The 1994 WTO Subsidies Agreement', reprinted in Gary Horlick (ed.), *WTO & NAFTA Rules and Dispute Resolution: Selected Essays on Antidumping, Subsidies and other Measures* (London: Cameron May Ltd, 2003), 21–38; Gary Horlick, Reinhard Quick & Edwin Vermulst, 'Government Actions Against Domestic Subsidies, An Analysis of the International Rules and an Introduction to United States' Practice', *Legal Issues of European Integration* 1 (1986): 1–51, reprinted in Gary Horlick (ed.), *WTO & NAFTA Rules and Dispute Resolution: Selected Essays on Antidumping, Subsidies and other Measures* (London: Cameron May Ltd, 2003), 39–100, at 42–63, with a particular focus on domestic subsidies under the GATT and the Subsidies Code. On services subsidies, see Pietro Poretti, 'Waiting for Godot: Subsidy disciplines in services trade', in GATS and the Regulation of International Trade in Services, eds Marion Panizzon & Nicole Poh & Pierré Sauvé (Cambridge/Newyork et al.: CUP, 2008), at 466–488.

[100] Finding a definition of subsidies under the GATT legal framework indeed proved to be an ambitious undertaking. See, *inter alia*, S. Alessandrini, 'Subsidies, Strategic Trade Policies and the GATT', in *Subsidies and International Trade*, ed. J.H.J. Bourgeois (Deventer: Kluwer Law and Taxation Publishers, 1991): 5–16; see also G. Depayre & R. Mauro Petriccione, 'Definition of Subsidy', in *Subsidies and International Trade*, ed. J.H.J. Bourgeois (Deventer: Kluwer Law and Taxation Publishers, 1991), 67–74.

[101] Historically, the US predominated as a user of countervailing duties. From 1995 to 2003, developed countries more generally stood out as implying countervailing duties. Such a development may be interpreted as illustrating the distinctive views of subsidies on an international level and the particularly limited international agreement on the status of subsidies as policy instruments. Trebilcock/Howse, above n. 20, at 262; see also Horlick/Quick/Vermulst, above n. 99, at 48–50.

any imported product of a contracting party and are held to be limited to the amount equal to the estimated bounty or subsidy determined to have been granted either in the process of manufacture, production, export, or transportation. The countervailing duties are addressed together with anti-dumping duties in Article VI of GATT 1994 because they both address 'below-normal value pricing'[102] of the products at issue.[103] However, a line of distinction is drawn between subsidization as a distorting government practice and dumping as a potential pricing policy of private market players.[104]

(2) Article III:8(b) excludes the payment of subsidies from the national treatment according to Article III of GATT 1994. It thereby encompasses subsidies to domestic producers, payments to domestic producers derived from the proceeds of internal taxes or charges, as well as subsidies effected through governmental purchases of domestic products. As a consequence, the terms of the General Agreement acknowledge the right of the contracting parties to adopt certain measures they deem necessary, for example, to foster economic development or to protect domestic industry.[105]

(3) With Article XVI of GATT 1994, the regulation of subsidies was sought to be strengthened under the General Agreement; at the time of the establishment of the GATT 1947, it only contained one provision, which was further expanded to encompass provisions on export subsidies in 1955 and, finally, in 1960, an illustrative list of export subsidies was included as an aid for interpretation.[106] Section A of Article XVI now addresses subsidies in general, thereby stating that parties granting or maintaining subsidies are held to notify the other contracting parties in writing 'of the extent and nature of the subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary'. The possibility of limiting such subsidization shall be subjected to discussion between the contracting parties concerned in the case that a parties' interests are affected by such measures. Section B of Article XVI focuses on export subsidies in particular, thereby providing for the general principle that the use of subsidies on the export of primary products should be avoided, in view of preventing subsidies to result in a contracting party having more than an 'equitable share' of world export trade in that particular product (Article XVI:3).[107] The

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[102] Trebilcock/Howse, above n. 20, at 263.

[103] Article VI:1 of GATT 1994 considers a product to be introduced into the commerce of an importing country at less than its normal value, 'if the price of the product exported from one country to another (a) is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country, or, (b), in the absence of such domestic price, is less than either (i) the highest comparable price for the like product for export to any third country in the ordinary course of trade, or (ii) the cost of production of the product in the country of origin plus a reasonable addition for selling cost and profit.'

[104] Trebilcock/Howse, above n. 20, at 263.

[105] See, e.g., GATT Panel Report, *Italian Discrimination Against Imported Agricultural Machinery*, BISD 7S/60, adopted 23 Oct. 1958, at para. 16.

[106] See Trebilcock/Howse, above n. 20, at 263–264 with further references; see also Horlick/Quick/Vermulst, above n. 99, at 42–47.

[107] The criterion 'more than equitable share' has been a disputed notion of the GATT system. For an overview, see Benitah, above n. 99, at 173–181 with reference to several cases adopted by the GATT Panel: GATT Panel Report,

mere encouragement of notification and consultation on the use of subsidies between Member States has not proven to be a very effective instrument to prevent subsidization. Moreover, the distinction between primary and non-primary products in section B of the provision was interpreted as discriminating against developing countries, which consequently did not endorse this section.[108] Despite having received a separate regulation within the General Agreement, Article XVI has thus been assessed as having granted subsidies a rather rudimentary provision.[109]

4.2.2. *Subsidies' Regulation in the SCM Agreement*

Efforts to address subsidization more effectively were undertaken and lead to a list of prohibited export subsidies in 1960. Furthermore, in light of the increased criticism against the US policies on countervailing duties, the US government decided to address the regulation of subsidies more generally during the Tokyo Round negotiations, a step that finally resulted in the 1979 Tokyo Round Code on Subsidies and Countervailing Duties.[110] This plurilateral agreement was particularly adopted by Organization for Economic Cooperation and Development (OECD) countries and a small number of advanced developing countries and expanded the existing GATT provisions considerably. It adopted a two-track approach, by addressing unilateral responses to subsidies, on the one hand, and multilateral regulation of subsidies, on the other hand.[111] In Article 11 of the Code, domestic subsidies were recognized as important and legitimate instruments and were thus permitted for the promotion of social and economic policy objectives. They could nevertheless be challenged if they caused (1) injury to the domestic industry of another signatory, (2) nullification or impairment of the benefits accruing to another signatory under the General Agreement, or (3) serious prejudice to the interests of another signatory. The challenge entailed a primary obligation of the complaining signatory to consult with the subsidizing country. Unless a mutually acceptable solution was achieved, a panel would be formed by the Committee on SCM, which could provide for specific recommendation to the parties. If such recommendations were not followed, the Committee could authorize countermeasures.[112]

Despite such international efforts, subsidization remained a contentious issue on the international trade agenda and was thus taken up again during the Uruguay Round.[113]

French Assistance to Exports of Wheat and Wheat Flour, BISD 7S/46, adopted 21 Nov. 1958; GATT Panel Report, *European Communities – Refunds on Exports of Sugar*, BISD 26S/290, adopted 6 Nov. 1979; GATT Panel Report, *European Communities – Refunds on Exports of Sugar Complaint by Brazil*, BISD 27S/69, adopted 19 Nov. 1980; GATT Panel Report, *European Economic Community – Subsidies on Export of Wheat Flour*, SCM/42, adopted 21 Mar. 1983.

[108] Jackson, above n. 90, at 286; see Trebilcock/Howse, above n. 20, at 263–264 with further references.

[109] Horlick/Quick/Vermulst, above n. 99, at 63–67 regarding domestic subsidies in particular.

[110] Agreement on Interpretation and Application of Arts VI, XVI, and XXIII of the General Agreement on Tariffs and Trade ('Subsidies Code').

[111] See Trebilcock/Howse, above n. 20, at 264–265 on the two-track approach; Jackson, above n. 90, at 288–290; Luengo Hernández de Madrid, above n. 99, at 63–74; see also Horlick/Quick/Vermulst, above n. 99, at 52–63.

[112] See Trebilcock/Howse, above n. 20, at 266.

[113] See Trebilcock/Howse, above n. 20, at 266.

During these negotiation rounds, the Agreement on SCM Agreement[114] was adopted, replacing the preceding legal situation by a comprehensive and rather detailed legal framework.

The SCM Agreement contains five main parts: Part I encompasses general provisions, thereby providing for a definition of the term 'subsidy' in its Article 1. Parts II, III, and IV of the SCM Agreement cover what is often referred to as the 'red, green, yellow light'[115] or the 'traffic light'[116] approach. Accordingly, subsidies may distinguished into three broad categories, namely, a 'prohibited (red)', an 'actionable (yellow)', and a 'non-actionable (green)' category. Prohibited subsidies encompass subsidies that are harmful to trade per se, whereas non-actionable subsidies receive 'green light' and are considered as being permitted.[117] The third category of actionable subsidies may be challenged if their effects on international trade are considered harmful. Part V of the SCM Agreement addresses countervailing duty measures. Notably, the category of non-actionable (green) subsidies is, however, no longer applicable. According to Article 31, non-actionable subsidies were limited to a period of five years starting with the entry into force of the WTO, not least because developing countries were afraid that the green category would be excessively used by industrialized countries. Time will tell whether they will be put back into force according to current efforts on the international stage.[118]

With the establishment of the SCM Agreement, the institutionalization of a Committee on SCM was adopted from the Tokyo Code and was realized in Part VI of the SCM Agreement (Article 24.1). The Committee is composed of representatives from the Member States and establishes a permanent group of five independent experts (the PGE), which can be requested to assist a panel and to elaborate advisory opinions on the existence and the nature of any subsidy (Article 24.3). Part VII of the SCM Agreement addresses notification and surveillance procedures with respect to subsidies; members are obliged to notify subsidies annually to the Committee (Article 25). According to Article 26, the Committee is obliged to examine the notifications in regular surveillance. Part VIII of the SCM Agreement entails special and differential treatment provisions for developing country members, in light of the fact that subsidization may play an important role for the economic development programmes of such countries (Article 27.1).[119] The SCM

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[114] Agreement on Subsidies and Countervailing Measures (SCM Agreement), 15 Apr. 1994, 1867 UNTS 14, <www.wto.org/english/docs_e/legal_e/24-scm.pdf> (visited 23 Jun. 2009).

[115] Jackson, above n. 90, at 290.

[116] Cottier/Oesch, above n. 36, at 993.

[117] Non-actionable subsidies could not be challenged under the SCM Agreement. However, in cases where a Member State had reasons to believe that serious adverse effects were to be expected for the domestic industry, the member was allowed to request consultations, and if no mutually acceptable solution was reached, the Member could refer the matter to Subsidies Committee, which had the responsibility to immediately review the facts and the evidence of the effects. The Committee could then recommend modifi cations to the subsidy programme in a way to remove the adverse effects. In cases where the recommendation was not followed within six months, the requesting member was authorized by the Committee to take appropriate countermeasures commensurate with the nature and degree of the effects determined to exist (see Art. 9 of the SCM Agreement).

[118] Cottier/Oesch, above n. 36, at 993.

[119] For example, the regulations on prohibited subsidies are exempted from application to least-developed countries, whereas other developing countries are provided with an eight-year grace period to comply with these provisions (Art. 27.4 of the SCM Agreement).

Agreement is then rounded off by Part IX on transitional arrangements, Part X covering Article 30 on dispute settlement, and Part XI with final provisions, as well as seven Annexes.

4.2.3. *Interim Conclusions*

In light of the ongoing Doha Round negotiations, the basic concepts and principles of both Article VI of GATT 1994 and of the SCM Agreement have been confirmed; nevertheless, their clarification and improvement are still envisaged.[120] At the Doha Ministerial Conference, WTO members agreed to launch negotiations in the area of 'WTO Rules', that is, on the subject matter of (1) the Agreement on Implementation of Article VI of GATT 1994 (the so-called Anti-dumping Agreement), (2) the Agreement on SCM, and the WTO disciplines on fisheries subsidies in particular, as well as (3) the WTO provisions applying to regional trade agreements.[121] New texts have been drafted in these specific fields to provide a common baseline for further discussions. However, in light of the difficulties to achieve consensus, a lot of work still needs to be done in order to achieve a coherent and enhanced framework.[122]

For the time being, both the GATT provisions and the SCM Agreement seek to balance the need for redistribution and implementation of legitimate policy goals with free trade principles.[123] The relationship between these legal frameworks was disputed. In the case of *Brazil – Measures Affecting Desiccated Coconut*,[124] the Appellate Body opined that GATT 1994 and the SCM Agreement form an inseparable package of rights and disciplines that must be considered in conjunction. Such an interpretation also corresponds to Article II:2 of the WTO Agreement, which clearly stipulates that 'the agreements and associated legal instruments included in the Annexes 1, 2 and 3 (hereafter referred to as "Multilateral Trade Agreements") are integral parts of this Agreement, binding all Members'; the SCM Agreement has been incorporated into Annex 1A on multilateral agreements on trade in goods of the WTO Agreement. In cases of conflict, the SCM Agreement supersedes the text of the GATT according to the general interpretative note included in Annex 1A of the WTO Agreement[125] and in light of the extensive and detailed provisions given by the SCM Agreement in terms of a *lex specialis*.[126]

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[120] WTO, Ministerial Declaration (2001), WTO Doc WT/MIN(01)/DEC/1 (Ministerial Conference, Fourth Session, Doha Declaration), at paras 28–29.

[121] WTO, Doha Work Programme, Ministerial Declaration (2005), WTO Doc. WT/MIN(05)/DEC (Ministerial Conference, Sixth Session), at para. 28 and Annex D.

[122] See, e.g., introductory statement to the WTO Negotiating Group on Rules, New Draft Consolidated Chair Texts of the AD and SCM Agreements, 19 Dec. 2008, WTO Doc TN/RL/W/236.

[123] Cottier/Oesch, above n. 36, at 990.

[124] WTO Appellate Body Report, *Brazil – Measures Affecting Desiccated Coconut*, WT/DS22/AB/R, adopted 21 Feb. 1997.

[125] *Ibid.*, 12–14, 17–18.

[126] See also Grave, above n. 99, at 97; Horlick/Clarke, above n. 99, at 21.

5. Critical Assessment of the Support of the Automobile Industry Under the GATT and the SCM Agreement

5.1. Defining subsidies

A subsidy is deemed to exist under the SCM Agreement if the criteria under Article 1 of the SCM Agreement are met.[127] Accordingly, a subsidy is defined as 'a financial contribution by a government or any public body within the territory of a Member' or 'any form of income or price support in the sense of Article XVI of GATT 1994' that confers a benefit.[128] The meaning of 'financial contribution' and 'benefit' has been the subject of appeal in several WTO cases.[129]

According to the Agreement's text, a 'financial contribution' is provided (1) where a government practice involves a direct transfer of funds or potential direct transfers of funds or liabilities, (2) where a government revenue that is otherwise due is foregone or not collected, (3) where a government provides goods or services other than general infrastructure or purchases such goods, and (4) where a government makes payments to a funding mechanism or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (1) to (3), which would normally be vested in the government and where the practice, in no real sense, differs from practices normally followed by governments.[130]

The manifold cases of governmental support of the automobile industry within different WTO Member States clearly amount to '*financial contributions*' in terms of Article 1.1(a)(1) of the SCM Agreement. The supporting measures adopted for the rescue of GM and Chrysler in the United States, for example, provided for direct transfers of funds, namely, of federal grants and loans, as well as considerable loan guarantees in light of attempts to promote research and innovation, that is, 'potential direct transfers of funds or liabilities' according to the terminology of the Agreement.[131] Furthermore, governments acquired preferred shares and thus directly transferred funds under the title of equity infusions; they have therefore become both acquirers and providers of

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[127] See Grave, above n. 99, at 133 with further references. See also *Id.*, above n. 99, at 124–257 on the subsidies' conceptualization in general as well as on different forms of subsidies; see also Luengo Hernández de Madrid, above n. 99, at 102–129. See also Gilbert Gangné & François Roch, 'The US-Canada Softwood Lumber Dispute and the WTO definition of subsidy', *World Trade Review* 7(2008): 547–572, at 556–568 on the approach taken in the Softwood lumber dispute in particular, which has influenced the present multilateral definition and continues to do so in the Doha round negotiations on subsidies.

[128] In WTO Panel Report, *Korea – Measures Affecting Trade in Commercial Vessels*, WT/DS273/R, adopted 7 Mar. 2005, at paras 7.50–7.56, 7.351–7.356, the Panel took different factors into account for conceptualizing a 'public body', such as the importance of the mandate of government-appointed officials, e.g., as well governmental control. Government ownership of 100% was seen as 'highly relevant to and often determinative of government control.'

[129] For a general overview, see Trebilcock/Howse, above n. 20, at 266–268; Cottier/Oesch, above n. 36, at 993–997.

[130] See Art. 1.1(a)(1) of the SCM Agreement. 'Entrustment' to a private body was explained by the AB as occurring where a government gives responsibility to a private body; 'direction' refers to situations of governmental exercise of its authority over a private body (see WTO Appellate Body Report, *United States – Countervailing Duty Investigation on Dynamic Random Access Memory Semiconductors (DRAMS) from Korea*, WT/DS296/AB/R, adopted 27 Jun. 2005, at para. 116). In the WTO Appellate Body Report, United States-Final Countervailing Duty Determination with Respect to certain Softwood Lumber from Canada, WT/DS257/AB/R, adopted 19 Jan. 2004, at paras 46–76 (herein after 'WTO Appellate Body Report, US-Softwood Lumber'), the Appellate Body held that the evaluation of the existence of a financial contribution requires consideration of the nature of the transaction through which economic value is transferred by a state.

[131] Article 1.1(a)(1)(i) of the SCM Agreement.

debtor-in-possession financing.[132] However, the governments' interferences in the companies' policies and the composition of their management cannot be construed as a subsidy; these measures did not entail any financial contributions, income, or price support and did not result in a benefit in terms of the Agreement.[133]

The reduction of taxation as an incentive for both car buyers and car dealers may arguably be interpreted as the granting of 'government revenue that is otherwise due', which is foregone or not collected, in terms of Article 1.1(a)(1)(ii) of the SCM Agreement. The definition of such kinds of support was addressed by the Appellate Body particularly in the *United States – Tax Treatment for Foreign Sales Corporations* case,[134] in which the Appellate Body interpreted the provision as implying that 'less revenue has been raised by the government than would have been raised in a different situation, or, that is "otherwise". Moreover, the word "foregone" suggests that the government has given up an entitlement to raise revenue that it could "otherwise" have raised'. The term 'otherwise due' was explained as entailing 'some kind of comparison between the revenues due under the contested measures and revenue that would be due in some other situation'.[135]

According to the Appellate Body Report, the basis of comparison for tax incentives granted to car buyers would thus have to be the rules of taxation of the sovereign state in question. Consequently, if a glance at the state's tax rules reveals that a particularly defined fee is owed to the state by car owners, for example, the exemption of this taxation as a means of incentive to buy cars could probably be interpreted as a financial contribution in terms of Article 1.1 of the SCM Agreement. Footnote 1 of the SCM Agreement clarifies that in accordance with Article XVI of GATT 1994 and Annexes I through III of the SCM Agreement, the exemption of exported products from duties or taxes, which are usually borne by like products destined for domestic consumption, as well as the remission of such duties or taxes in amounts not in excess of those that have accrued, are not deemed to be a subsidy. Tax incentives levied for the enhancement of car exports, for example, would thus not necessarily fall under the scope of the Agreement.[136]

Furthermore, price-supporting measures adopted to increase car exports or reduce car imports according to Article XVI of GATT 1994 would also be deemed 'financial contributions' under Article 1.1(a)(2) of the SCM Agreement.

In addition to a 'financial contribution', the definition of a subsidy presumes a '*benefit*' in terms of Article 1.1(b) of the SCM Agreement.[137] Such a benefit has been

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[132] See GM Press Release, above n. 10; Simon, above n. 70.

[133] See also Grave, above n. 99, at 250 et seq. Furthermore, 'Cash for Clunkers' programs (see above n. 85) and tax credits for car purchases do no qualify as subsides because they do no confer benefits to domestic firms (see Brunel & Hufbauer, above n. 16, at 3).

[134] WTO Appellate Body Report, *United States – Tax Treatment for 'Foreign Sales Corporations'*, WT/DS108/AB/R, adopted 24 Feb. 2000.

[135] *Ibid.,* para. 90. See also paras 8.6–8.7.

[136] On the interpretation of footnote 1 to the Agreement, see, e.g., WTO Appellate Body Report, *Canada – Certain Measures Affecting the Automotive Industry* (hereinafter 'WTO Appellate Body Report *Canada-Autos*'), WT/DS139/AB/R, WT/DS142/AB/R, adopted 31 May 2000, where an import duty exemption, which was available to manufacturers of motor vehicles, was ruled as a prohibited subsidy in terms of Art. 1.1(a)(1)(ii) and Art. 3.1(a) of the Agreement.

[137] In WTO Appellate Body Report, *Brazil – Export Financing Programme for Aircraft*, WT/DS46/AB/R, adopted 2 Aug. 1999, at para. 157, the AB emphasized that the definitions of 'financial contribution' and 'benefit' should be distinguished 'as two separate legal elements in Art. 1.1 of the SCM Agreement which *together* determine whether a subsidy *exists*' [emphasis adopted from the original wording].

found to exist when a financial contribution is provided 'on terms that are more advantageous than those that would have been available to the recipient on the market'.[138] In the *Canada – Civilian Aircraft Case*, the Panel referred to Article 14 of the SCM Agreement as providing for valuable guidelines for calculating 'the benefit to the recipient conferred pursuant to paragraph 1 of Article 1', even though Article 14 applies in the context of Part V, that is, countervailing measures in response to subsidies granted, and expressly determines when an Article 1.1 'benefit' does not arise.[139] The Appellate Body adopted this approach[140] and added that 'benefits' do not exist in the abstract but must rely on the existence of a beneficiary or a recipient, which can either be 'a person, natural or legal, or a group of persons'.[141]

The subsidization of the automobile industry as such entails significant implications for other industry branches, such as the suppliers of individual car parts, as well as metal, coating, or tyre producers, for example. From their perspective, the support of car producers ensures the purchasing power of their customers. Arguably, this could amount to an *indirect* subsidization of the car producers also according to Article VI:3 of GATT 1994, due to the fact that they are not forced to decrease the market prices for their products according to reduced demands but manage to sustain high prices with widespread effects.[142]

The supported auto industry enterprises and the auto suppliers arguably constitute the subsidy recipients for the purpose of our exemplary case. The governmental support of 'the auto industry' as such may suffice to delineate the beneficiaries in question. According to Article 14(b) of the SCM Agreement, the granting of loans by a government can only be considered as conferring a benefit, if there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee. The benefit thus results from the difference between these two amounts adjusted for any differences in fees. Comparable guidelines are provided by Article 14(a) on the government provision of equity capital.

Against the background of the current economic crisis and resulting difficulties for real economy branches, comparing the parameters of 'the terms… that would have been

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[138] This is often referred to as the 'private investor test' according to WTO Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft* (hereinafter 'WTO Appellate Body Report, *Canada-Aircraft*'), WT/DS70/AB/R, adopted 2 Aug. 1999, at para. 157. See also WTO Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft* (hereinafter 'WTO Panel Report, *Canada-Aircraft*'), WT/DS70/R, adopted 14 Apr. 1999, at para. 9.112. See also Benitah, above n. 99, at 90–91, interpreting this approach as being inspired by the simple view of 'distortion' of the natural market mechanisms within a national economy.

[139] WTO Panel Report, *Canada-Aircraft*, above n. 138, at para. 9.113.

[140] WTO Appellate Body Report, *Canada-Aircraft*, above n. 138, at para. 155.

[141] *Ibid.,* para. 154; see further attempts to frame the definition of 'benefit' provided by Benitah, above n. 99, at 214–218 with further references; see also Grave, above n. 99, at 170–189.

[142] Indeed, the case law provided on 'indirect subsidies' did not specify an applicable definition. Nevertheless, it should be taken into account that indirect subsidies were usually considered in 'reversed' 'upstream cases'. For example, in GATT Panel Report, *United States – Countervailing Duties on Fresh, Chilled and Frozen Pork from Canada*, BISD/38S/30, adopted 11 Jul. 1991, the subsidies paid to producers of swine were interpreted as amounting to an indirect subsidization of exported pork meat. See Benitah, above n. 99, at 269–272. See also the WTO Appellate Body Report, US-Softwood Lumber, above n. 130, at paras 148–166, where the Appellate Body stated that before being entitled to impose countervailing duties, a state must assess whether the benefit has been 'passed through'. See Gagné & Roch, above n. 127, at 557–563.

available to the recipient on the market' and the terms provided in effect by the governments seems questionable and rather misleading due to the fact that comparable amounts of resources for the automobile industry would probably not have been available from private investors over the general market. As a consequence, it has been alleged that the only thinkable 'rescuer' in the present context could have been the state. Furthermore, in light of the considerable government interventions into the existing markets, it could now be contended that it has become difficult if not almost impossible to determine a market value, based on an undistorted equilibrium between supply and demand in a free market.

A comparable argument was brought forward by the United States in the *Canada – US Softwood Lumber Dispute*,[143] asserting that it was not possible to assess the adequacy of the remuneration on the basis of in-country prices, in light of the government's complete domination of the stumpage market at issue. This fact was said to make it impossible to use the small amount of private stumpage prices as a basis for any comparison. As a consequence, the United States opined that the private market prices of timber were not reflective of the 'fair market value' of timber in Canada.[144] The Panel interpreted the text of Article 14 of the SCM Agreement as not in any way qualifying the market conditions as such that are to be used as a benchmark. According to the Panel's decision, the legal text does not explicitly refer to a 'pure' market, a market 'undistorted by government intervention'. Moreover, the applicable paragraph (d) of Article 14 of the SCM Agreement identifies the market conditions that are to be used 'to determine adequacy of remuneration as those which are prevailing' in respect of the price of the good, its quality, availability, marketability, transportation, and other conditions of purchase or sale, in other words, the market conditions 'as can be found'. The Panel thus acknowledged no justification for disregarding the prevailing market prices on the grounds that they were distorted;[145] the United States were found in violation of Article 14 by not using Canadian private prices in their benefit calculations and in violation of Articles 10 and 32.1 for imposing countervailing duties based on such calculations.[146] The Appellate Body questioned these findings of the Panel and finally reversed them, particularly in view of the arguments regarding market distortions and the resulting effects on the prices in question. It interpreted Article 14(d) as permitting 'investigating authorities to use a benchmark other than private prices in that market' when private prices are distorted.[147] The Appellate Body agreed that alternative methods for determining the adequacy of remuneration in accordance with Article 14 'could include proxies that take into account prices for similar goods quoted on world markets, or proxies constructed on the basis of production costs.' However, it did not suggest alternative procedures for determining private prices and thus did not make any findings on the WTO consistency of any of these methods in the abstract.[148]

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[143] WTO Panel Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* (hereinafter 'WTO Panel Report, *US-Softwood Lumber*'), WT/DS257/R, adopted 29 Aug. 2003; WTO Appellate Body Report, *US-Softwood Lumber,* above n. 130.

[144] WTO Panel Report, *US-Softwood Lumber*, above n. 143, at para. 7.44.

[145] *Ibid.,* para. 7.51.

[146] *Ibid.,* para. 7.65.

[147] WTO Appellate Body Report, *US-Softwood Lumber*, above n. 130, at paras 100–103.

[148] *Ibid.,* para. 106. See also Gagné & Roch, above n. 127, at 555–557.

Although an undistorted market value is very difficult to attain given the present developments, it would be rather complicated to find another benchmark applicable in the current context of governmental market interventions. Nevertheless, it can be assumed that the governments' financial contributions were conceded on comparably beneficial terms regarding the fixed duration of the loans and the agreed interest rates, due to the governmental participation's extraordinary basis in light of an assumed case of emergency, making economic market considerations recede behind the priority objective of supporting the specific industry branches. Indeed, the interest rate on US loans of 5% exceeds London Interbank Loan offered Rate (LIBOR) by 3%.

As a consequence, and without overruling the considerations that remain necessary on a case-by-case basis, it seems appropriate to address the financial contributions granted to the automobile industry in light of the economic crisis as amounting to benefits and thus constituting subsidies under the SCM Agreement.

5.2. Specificity under the SCM agreement

In order for a subsidy to be prohibited under Part II, actionable under Part III or subjected to countervailing measures under Part V of the SCM Agreement, the subsidy in question has to be 'specific' in accordance with Article 2 of the Agreement.[149]

'Specific subsidies' according to the Agreement means that the subsidy has to be 'specific to an enterprise or industry or group of enterprises or industries' within the jurisdiction of the granting authorities. Thereby the limitation of subsidies 'to certain enterprises located within a designated geographical region within the jurisdiction of the granting authority'[150] is deemed to suffice for the purpose of the Agreement. However, even in such cases, a subsidy will not be considered 'specific' if the granting authority or the legislation pursuant to which the granting authority operates establishes objective criteria or conditions governing the eligibility for and the amount of a subsidy.[151] According to footnote 2 of the Agreement, objective criteria or conditions are interpreted as meaning criteria or conditions that are neutral (due to the fact that they do not favour certain enterprises over others) and that are economic in nature and apply horizontally. The Agreement names the number of employees or the size of the enterprise as examples for such non-specific criteria and conditions. These have to be clearly spelled out in a law, a regulation, or another official document, so as to be capable of verification and for the purpose of falling under Article 2.1(b) of the SCM Agreement. Notwithstanding any non-specificity according to the previous examination, Article 2.1(c) of the SCM Agreement rounds off the provision, by stipulating that if there are reasons to believe that the subsidy is *in fact* specific, other factors can be considered. Such factors may be the 'use of a subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportion-

[149] Article 1.2 of the SCM Agreement. See also Grave, above n. 99, at 189–210 and Luengo Hernández de Madrid, above n. 99, at 129–142 with an overview on the specificity criterion.

[150] Article 2.1(a) of the SCM Agreement.

[151] Article 2.1(b) of the SCM Agreement.

ately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy.'[152]

The policy arguments supporting such a specificity test can be distinguished into two main approaches, based on what is deemed a 'distortion' in international trade.[153]

First, seen from an economic angle, it seems that subsidies provided 'across the board to all of society and all of the producing sectors of society' do generally not distort the markets; if they do, their distorting effects may normally be considered as quite minimal.[154] On the contrary, *specific* subsidies are perceived as 'distorting' due to their impact on the production costs of firms having selectively received a subsidy. This leads to:

> [A]rtificial overproduction of subsidized products compared to what these firms would have chosen to produce, if the price of subsidized products had been able to reflect their real cost of production.(…) At the same moment [there is] in that economy an underproduction of other products more valuable socially, due to the fact that scarce productive resources have been artificially drained towards the manufacture of subsidized goods.[155]

In other words, the 'unfairness' of the subsidies is traced back to the distortion of natural comparative advantages between countries.[156]

Second, narrowing the focus on actionable subsidies by means of presupposing their specificity may provide for a useful tool of administration to omit general activities that all governments undertake, including societal infrastructure such as police, roads, schools, and so forth from a countervailing duty process.[157]

If the financial support of the automobile industry is not conferred to specific enterprises such as GM and Chrysler in the US but is granted to the 'automobile industry' as such, the question arises whether this would provide for sufficient specificity, particularly in view of the wide field encompassed by this market branch, which affects different subsectors such as markets for tyres, metals, motors, paint, etc.[158] For example, if the EU would decide to financially support the automobile industry as such on a regional level and the benefits were granted based on objective criteria or conditions, clearly spelled out in law and based on economic considerations, and if they were applicable horizontally, Article 2.1(b) of the SCM Agreement would have to be distinguished from paragraph (c) of the same provision. For the time being, the EU has indeed focused on outlining guidelines to support the automobile sector,[159] thereby leaving actual implementation to the Member States on a national level. In view of the de facto factors addressed by Article 2.1(c), which already accept the predominant use of a subsidy programme by

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[152] Article 2.1(c) of the SCM Agreement.

[153] On different views of 'distortion' see Benitah, above n. 99, at 252–280.

[154] Jackson, above n. 90, at 296–297; see also Grave, above n. 99, at 193–194, with a more critical approach, arguing that distortions of competition also occur when industry branches as such are subsidized, thereby referring to the first sentence of Art. 2.1 of the SCM Agreement.

[155] Benitah, above n. 99, at 89–90.

[156] *Ibid.,* 68.

[157] Jackson, above n. 90, at 297.

[158] See Jackson, above n. 90, at 298 with corresponding concerns regarding the agricultural sector and suggesting a 'distortion test' for constraining the breadth of a subsidy definition with a focus on whether a subsidy actually distorts economic activity compared with 'free market conditions'.

[159] For example, with the adoption of the Communication from the Commission – Responding to the crisis in the European automotive industry, above n. 59.

certain enterprises as providing for sufficient reasons to believe that a subsidy is specific, cases of non-specificity according to Article 2.1(b) of the SCM Agreement will arguably, however, remain the exception. In the present discussions, the financial benefits that hit the headlines were granted to individual enterprises; their specificity can be assumed.

5.3. Prohibited subsidies

Prohibited non-agricultural subsidies according to Article 3 of the SCM Agreement exist, where (1) subsidies are contingent, in law or in fact – whether solely or as one of several other conditions, upon export performance – including such cases as illustrated in Annex I, and where (2) subsidies are contingent upon the use of domestic over imported goods.

Both categories of subsidies entail distortions of competition, their specificity is thus perceived as a legal consequence of the classification as a prohibited subsidy, not as their prerequisite.[160] Annex I contains the Illustrative List of Export Subsidies, which provides for valuable guidance for assessing prohibited export subsidies.[161] Footnote 4 provides for the explanatory reasoning that contingency 'in fact' on export performance is met in cases where subsidies are 'tied to actual or anticipated exportation or export earnings'. The explanatory note continues by stating that 'the mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision'. The distinction between de facto and de jure contingency was particularly tackled in the *Canada-Aircraft Case*, in which the Appellate Body generally stated that the contingency expressed within the provision must be the same for both de facto and de jure contingency.[162] However, the evidence used for proving each differs considerably. While de jure contingency is demonstrated on the basis of the text of the applicable legal instrument, proving de facto export contingency will generally be a more complex undertaking.[163]

The second paragraph of Article 3 of the SCM Agreement addresses domestic content subsidies, that is, subsidies that aim at reducing imports of products from other countries and thereby favour domestic production.[164]

The real economy support in light of the financial deteriorations with the main objective of stabilizing the economy branches is not prohibited as such. Moreover, a particular leeway exists for establishing financial benefits under Article 3 of the SCM

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[160] See Grave, above n. 99, at 209–210 with further references; see also Horlick/Clarke, above n. 99, at 25–26.

[161] On the relationship between Art. 3.1(a) of the SCM Agreement and the Illustrative List see Dominic Coppens, 'How Much Credit for Export Credit Support under the SCM Agreement?', *Journal of International Economic Law* 12 (2009): 63–113, at 91–97.

[162] WTO Appellate Body Report, *Canada-Aircraft*, above n. 138, at paras 167–173; see also WTO Appellate Body Report, *Canada-Autos*, above n. 136.

[163] *Ibid.,* para. 167; on the 'in fact tied' criterion, see also Benitah, above n. 99, at 190–198; see Luengo Hernández de Madrid, above n. 99, at 144–148 on the distinction between de jure and de facto contingency and at 142–158 with an overview over prohibited subsidies.

[164] By addressing both domestic and export subsidies under the same provision, the SCM Agreement has abandoned the contentious distinction between the two types of subsidies adopted under Art. XVI of the GATT in particular. (See Luengo Hernández de Madrid, above n. 99, at 47 et seq. and at 154–155; Horlick/Quick/Vermulst, above n. 99, at 42–50; Grave, above n. 99, at 66 et seq., 84–87, and 128–129.)

Agreement. As long as the subsidies provided are not made contingent upon high export performances of a particular enterprise or industry or upon the use of domestic over imported goods – for example, within the production process, which would eventually result in a better treatment of the domestic industries – they are generally not prohibited under the SCM framework. In light of these findings, the so-called Buy American clause incorporated into the American Recovery and Reinvestment Act of 2009 regarding funds for the support of the iron and steel industry[165] could turn out to be problematic; it stipulates that the funds made available by the US government can only be used 'for a project for the construction, alteration, maintenance, or repair of a public building or public work unless all of the iron and steel used in the project is produced in the United States'. The tensions such a clause could provoke has been acknowledged, leading to an adjustment of the provision to state that the clause:

> shall not apply in any case or category of cases in which the head of the Federal department or agency involved finds that (1) applying subsection (a) [the clause] would be inconsistent with the public interest; (2) iron, steel, and the relevant manufactured goods are not produced in the United States in sufficient and reasonably available quantities and of a satisfactory quality; or (3) the inclusion of iron, steel, and manufactured goods produced in the United States will increase the cost of the overall project my more than 25 percent.

Most notably, it is held that 'this section shall be applied in a manner consistent with United States obligations under international agreements'. Similar concerns have been raised with regard to France's announcement of making aid to the automative sector conditional on automakers' maintaining their production on French grounds and purchasing certain parts from French suppliers, as well as forestalling the export of jobs to other countries, such measures would violate EU rules, however, France has committed to avoid any breaches of Internal Market Principles.[166] It remains to be seen how such clauses can be applied in conformity with the WTO legal framework.

5.4. Actionable subsidies

Actionable subsidies are regulated in Part III of the SCM Agreement. Exempted from the actionable subsidies' scope of application are the subsidies maintained on agricultural products according to Article 13 of the Agreement on Agriculture. Apart from this exception, subsidies are framed as addressing specific forms of government assistance to firms or industries and are objectionable if *adverse effects* to the interests of other members are caused. Such adverse effects may consist in (1) the injury to the domestic industry of another member; (2) the nullification or impairment of benefits accruing

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[165] It held 'for a project for the construction, alteration, maintenance, or repair of a public building or public work unless all of the iron and steel used in the project is produced in the United States' (s. 1605 of the American Recovery and Reinvestment Act of 2009, HR1).

[166] See Brunel & Hufbauer, above n.16, at 5, 8. See also EU Presse Release, State aids: the Commission obtains guarantees from the French governments on the absence of protectionist measures in the French plan for aid to the automotive sector, Brussles, 28 Feb. 2009, MEMO/09/90; Report from the Commission – State Aid Scoreboard, Spring 2009 update, Special Edition on State Aid Interventions in the Current Financial and Economic Crisis, 8 Apr. 2009, COM(2009) 164, at 26.

directly or indirectly to other members under the GATT 1994, including the benefits of concessions bound under Article II of GATT 1994; or (3) in the serious prejudice to the interests of another member.[167]

In the present situation of governmental support granted to the automobile industry, adverse effects resulting either from *material injury to the domestic industry of another Member* (Article 5[a]) or *serious prejudice to the interests of another Member* (Article 5[c]) are potentially given and will be further examined.

5.4.1. *Defining the Market: Like Products*

As a starting point for assessing cases of actionable subsidies, the preliminary and fundamental question needs to be addressed, which '*like products*' shall be compared. According to footnote 46 of the SCM Agreement, the term 'like product' is interpreted as meaning 'a product which is identical, that is, alike in all respects to the product under consideration, or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration'. Although the term 'like product' is used in a variety of contexts within the WTO Agreement, the SCM Agreement adopts its own definition of the term.[168] Framing the comparable products and their markets and thus the industry in question is of central importance for taking the second step of identifying cases of material injury or serious prejudice. Indeed, 'the more narrowly the domestic market is defined, the greater the likelihood of an affirmative injury finding'.[169]

As a consequence of this contribution's focus on the 'automobile industry', the products subject to further assessment are 'automobiles'. This term covers different vehicles and therewith raises the question whether such automobiles, after all produced for different customers, should be compared as like products. If no identical products are at hand, a wide range of criteria may help assess which automobiles have 'characteristics closely resembling' one another. These include the physical characteristics of the vehicles in question, such as their size, weight, height, engine size and capacity, safety features, and so forth, as well as other factors such as the automobiles' brands, their image/reputation, status and resale values, their price and tariff classification, as well as their end-use.[170] Furthermore, helpful inputs may be provided by the market segmentation adopted by the automotive industry itself, an approach adopted by the Panel in *Indonesia – Certain Measures Affecting the Automobile Industry*.[171] Indeed, passenger cars are generally highly differentiated products; depending on the compared objects, huge price differences may

[167] Article 5 of the SCM Agreement.

[168] WTO Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry* (hereinafter 'WTO Panel Report, *Indonesia-Autos*'), WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, adopted 2 Jul. 1998, at para. 14.170.

[169] Bruce M. Steen, 'Economically Meaningful Markets: An Alternative Approach to Defining "Like Product" and "Domestic Industry" under the Trade Agreements Act of 1979', *Virginia Law Review* 73 (1987): 1459–1499, at 1470.

[170] WTO Panel Report, *Indonesia-Autos*, above n.168, at paras 14.165–14.173. In this case, the Panel held that the definition of 'like products' given in footnote 46 of the SCM Agreement does not preclude the analysis of other criteria other than physical characteristics (*Id.*, at para. 14.173).

[171] WTO Panel Report, *Indonesia-Autos*, above n. 168, at paras 14.177–14.193.

exist between brands and models resulting in rather low degrees of substitutability. Particularly in light of the governments' tendency to promote 'green' industry developments, the question arises whether fuel-efficient cars are 'like' large sport utility vehicles (SUV) or whether a distinction should be made, resulting, for example, in the increased support of green cars over others. If 'automobiles' are perceived widely as motor-driven vehicles for land use that do not cover rail vehicles, it seems clear that both 'green' and polluting cars would be encompassed. Convincing arguments can be invoked in favour of such an approach. Due to the fact that particularly the US government's support is supposed to benefit former producers of SUVs in order to provide for incentives for their change of thinking as potent automobile suppliers, a distinction between the same producers' goods based on environmental considerations could be perceived as rather artificial.[172] Nevertheless and despite such theoretical observations, an effective assessment and comparison can only be made on a case-by-case basis, whereby the analysis of 'like products' under other WTO law provisions can provide for valuable guidance.[173]

5.4.2. *Injury to the Domestic Industry*

5.4.2.1. *Defining material injuries*

'Injury to the domestic industry' is interpreted according to Part V of the SCM Agreement, that is, Article 15 in particular,[174] and can also be read in the light of Article VI of GATT 1994.[175] Footnote 45 defines 'injury' as meaning 'material injury to a domestic industry, threat of material industry or material retardation of the establishment of such an industry'. The term shall be interpreted in accordance with the provisions of Article 15 of the SCM Agreement. Thereby, a threat of material injury is to be based on facts 'and not merely on allegation, conjecture or remote possibility'. Furthermore, the change in circumstances that is deemed to create such an injuring situation 'must be clearly foreseen and imminent'. The investigating authorities are held to consider *inter alia* such factors as the nature of the subsidy, a significant rate of increase of subsidized imports, or the prices of the imports in question, 'in making a determination regarding the existence of a threat of material injury'.[176] According to Article 15.1 of the SCM Agreement, positive evidence is required for determining injury, which includes an objective examination of two criteria, namely, (1) the volume of the subsidization and the effect of the subsidized products on prices in the other member's market for like products and (2) the consequent impact of these subsidizations on the other member's producers of such

[172] See also WTO Panel Report, *Indonesia-Autos*, above n. 168, at paras 14.140–14.193.
[173] WTO Panel Report, *Indonesia-Autos*, above n. 168, at para. 14.174.
[174] Footnote 11 of the SCM Agreement.
[175] Article VI:6(a) of GATT 1994 stipulates that: 'No contracting party shall levy any (…) countervailing duty on the importation of any product of the territory of another contracting party unless it determines that the effect of the (…) subsidization (…) is such as to cause or threaten material injury to an established domestic industry or is such as to retard materially the establishment of a domestic industry.'
[176] Article 15.7 of the SCM Agreement.

products.[177] The investigating authorities are thus held to consider whether there has been a significant increase in subsidization, in absolute or relative terms, that is, relative to the production or consumption in the other Member State. A strong effect is deemed to exist where there has been a significant price undercutting by the subsidization as compared with the price of a like product experiencing no governmental support.[178] Furthermore, the examination of the impact of the subsidies in question on the industry producing like products, includes:

> an evaluation of all relevant economic factors and indices having a bearing on the State of the industry, including actual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments' etc.[179]

A precise technical definition of the concept of 'injury' is thus not provided by the SCM Agreement, which relies on a list of elements that should be examined in an objective manner for establishing 'injury' on a case-by-case basis. Investigating authorities are therefore rather free to evaluate the relative weight of each element in a given case.[180]

5.4.2.2. *Causality between subsidy and injury*

A particular difficulty arises from the necessity to demonstrate that the subsidies in question cause the injuries, thus that a causal relationship between the subsidies and the injury exists. This prerequisite results from the wording of Article VI of GATT 1994, as well as Article 15.5 of the SCM Agreement.[181] Accordingly, the causal relationship is based on the national authorities' examination of all relevant evidence and any *other* factors (that is, other than the subsidized imports) that may cause material injuries to the domestic industries. These are, *inter alia*, the volume and prices of non-subsidized imports of the same product in question, contraction in demand or changes to the patterns of consumption, trade restrictive practices and competition between the foreign and the domestic producers, development in technology, and the export performance and productivity of the domestic industry. According to the Panel's interpretation of this second sentence in the *Panel on Canadian Countervailing Duties on Grain Corn from the United States* case,[182] assuming causality between a subsidy and an injury was to be avoided in

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[177] See Art. 15.2 of the SCM Agreement, which, in its original wording, refers to subsidized *imports* due to its primary application on countervailing duties, which are imposed on products stemming from the territory of a Member State and are imported into the territory of another.

[178] See Art. 15.2 of the SCM Agreement. See also for further valuable inputs Art.VI:1 of GATT 1994 for the evaluation of below-normal value pricing.

[179] Article 15.4 of the SCM Agreement.

[180] Benitah, above n. 99, at 14 with particular reference to Gary Clyde Hufbauer & Johanna Shelton Erb, *Subsidies in International Trade* (Washington, DC: Institute for International Economics/Cambridge, Massachusetts: MIT Press, 1984), at 24 on Art. 6:3 of the Tokyo Subsidies Code.

[181] See also Art. 15.1 of the SCM Agreement referring to the GATT provision, Art. 15.2 and Art. 15.4 of the SCM Agreement.

[182] GATT Panel Report, *Panel on Canadian Countervailing Duties on Grain Corn from the United States*, BISD 39S/411, adopted by the Committee on Subsidies and Countervailing Measures on 26 Mar. 1992.

cases where all the appearances of an injury seemed to be caused by a subsidized import, however, where in actual fact, the real and exclusive cause was related to factors other than subsidies. In this case where a dramatic decline in world market prices for grain corn occurred, the Panel reasoned that producers would have been affected even in the absence of subsidized imports.[183]

The necessity to prove a causal relationship between the subsidy and the injury has been criticized as resulting in a legally indeterminate text. With Article 15.5 of the SCM Agreement's reference to Articles 15.2 and 15.4 according to footnote 47, the causal requirement was interpreted as becoming redundant, due to the fact that the determination of the existence of an injury, according to a text-based interpretation of paragraphs 2 and 4 of the provision, 'is at the same time a demonstration of the causal relationship between the subsidized imports and the injury, through the effects of the subsidies'.[184] Linked to this finding is the related question whether 'the effects of the subsidized imports' and 'the effects of the subsidy' are equivalent.[185] However, based on a more teleological interpretation of Article 15.5 of the SCM Agreement and by stretching the literal meaning of footnote 47, it is possible to interpret the provision as examining the factors mentioned in paragraphs 2 and 4 and thus considering the effects of the subsidy for the interpretation of causality; references to the effects do not guarantee the fulfilment of the obligation in the first sentence of Article 15.5 of the SCM Agreement.[186]

For the purpose of assessing the subsidization of the auto industry, different aspects should be considered for scrutinizing a causal relationship between the subsidy and the alleged injury at hand. The substantial amounts of governmental sources that have been granted to the automobile sector arguably result in considerable effects that such subsidization may have regarding imports and prices of automobiles. According to Article 15.5 of the SCM Agreement, the current economic crisis also needs due consideration. Indeed, the support of the automobile industry has been undertaken in times in which market distortions seem to accompany the deteriorations as a rather common feature and the demand-side of auto-buyers is naturally decreasing due to financial losses; the volumes and prices for automobiles are adjusted in a corresponding downwards manner. It is only in light of such findings that a fairly adequate picture can be framed and the question can be answered on a case-by-case basis whether, according to an ordinary run of events, a corresponding subsidy would have lead to an according injury.

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[183] *Ibid.,* para. 5.2.9; see also Benitah, above n. 99, at 287. In other words, the subsidy in question was not a '*conditio sine qua non*' and thus not a necessary prerequisite for the occurrence of the injury that would otherwise not have come to effect.

[184] Benitah, above n. 99, at 283–284; for a more general overview, see *Id.*, at 281–304.

[185] See Benitah, above n. 99, at 300–304, focusing particularly on the case of GATT Panel Report, *United States – Imposition of Countervailing Duties on Imports of Fresh and Chilled Atlantic Salmon from Norway*, SCM/153, adopted by the Committee on Subsidies and Countervailing Measures on 28 Apr. 1994.

[186] See also Benitah, above n. 99, at 285–286 with further references.

5.4.3. *Serious Prejudice to the Interests of Another State*

5.4.3.1. *Framing cases of serious prejudice*

Actionability of the subsidies in question may also derive from cases where the adverse effects caused consist in serious prejudice to the interests of another member (Article 5[c] of the SCM Agreement). Article 6 of the SCM Agreement particularly explains the notion of 'serious prejudice', which is only assumed the subsidy has resulted in an effect listed in paragraph 3 to the provision.[187] This is the case if either one or several of the following situations apply:

(1) the effect of the subsidy is to displace or impede the *imports* of a like product of another member into the market of the subsidizing member;
(2) the effect of the subsidy is to displace or impede the *exports* of a like product of another member from a third country market;
(3) the effect of the subsidy is a significant price undercutting by the subsidized product as compared with the price of a like product of another member in the same market or significant price suppression, price depression or lost sales in the same market;
(4) the effect of the subsidy is an increase in the world market share of the subsidizing member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.[188]

Article 6.4 of the SCM Agreement elucidates that the displacement or impediment of exports includes any cases in which it can be demonstrated that a change in relative shares of the market has resulted as a disadvantage of the non-subsidized like product. This may be the case if there is an increase in the market share of the subsidized product, if the market share of the subsidized product remains constant although circumstances exist according to which the shares would have declined in the absence of the subsidy, as well as if the market share drops but at a slower rate than would have been the case without the subsidy. Such developments are examined over a representative period of time that is deemed sufficient to demonstrate clear trends in the development of the concerned product market, that is, 'in normal circumstances', at least one year. Article 6.5 of the SCM Agreement annotates that a price undercutting in terms of paragraph 3(c) is assessed by means of comparing the prices of the subsidized product with prices of non-subsidized like products supplied to the same market. If a direct comparison is not possible, export unit values may be examined to demonstrate the existence of such price undercutting.[189]

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[187] See Art. 6.2 of the SCM Agreement.
[188] Article 6.3 of the SCM Agreement (emphasis added).
[189] See, e.g., WTO Appellate Body Report, *United States – Subsidies on Upland Cotton Recourse to Article 21.5 of the DSU by Brazil*, WT/DS267/AB/RW, adopted 2 Jun. 2008, at para. 368, in which the Appellate Body accepted the Panel's 'but for' approach, which it understood as requiring that price suppression be the effect of the subsidies at issue and that

Article 6.7 of the SCM Agreement establishes particular exceptions to the presumption of a displacement or impediment resulting in serious prejudice. This may be the case where the complaining member has adopted similar measures, for example, resulting in a prohibition or restriction on exports of the like products, as well as in the event of natural disasters, strikes, transport disruptions, or other 'force majeure', which substantially affect the product's production, qualities, quantities, or prices. In such cases, the adverse effects to the interests of the complaining member do not seem to be established.

For the purpose of this examination, the question whether the governmental support provided to the automobile sector results in one or various of the effects as listed in Article 6.3 of the SCM Agreement should particularly focus on whether a change in relative market shares can be observed, whether prices are undercut, or whether an increase in the world market share of the subsidizing member can be assessed. In the current situation, it is important to take into account the potent market power and the global market shares that the affected automobile producers have gained over the years. GM, Ford, and Chrysler have often been referred to as the 'Big Three'. In this position, the most powerful automobile producers already had a substantial impact on the price determination without governmental support. The challenge would thus be to examine the *government's* effect in particular. Furthermore, the question would have to be tackled which period of time should be examined to demonstrate the trends at issue. While Article 6.4 of the SCM Agreement asks for a minimal period of at least one year 'in normal circumstances', solid arguments would probably opt for a different representative time period in light of the exceptional situation as is currently experienced. In light of such considerations, the distinction between short-termed and long-termed governmental measures has to be taken into account. This is also the case in view of Article 6.1 of the SCM Agreement listing four cases where serious prejudice is deemed to exist. Although this provision is no longer applicable, it is interpreted as nonetheless providing for some guidance for the understanding of the original architecture of the Agreement[190] and shall thus be adopted accordingly.

Regarding the current measures supporting the automobile sector, particularly two cases of serious prejudice can be distinguished: on the one hand, subsidies have been granted to cover operating losses sustained by the particular industries in the automobile sector (Article 6.1[b]), on the other hand, subsidies have also been granted to cover losses sustained by individual enterprises (Article 6.1[c]). This distinction is important, because subsidies towards enterprises may be justified in cases in which they are deemed to result in 'one-time measures which are non-recurrent and cannot be repeated for that

there be a 'genuine and substantial relationship of cause and effect' between the subsidies in question and the price suppression. See also WTO Panel Report, *Indonesia-Autos*, above n. 168, at paras 14.237–14.257 with an analysis of Art. 6.3(c) of the SCM Agreement.

[190] WTO Decision by the Arbitrator, *United States – Tax Treatment for 'Foreign Sales Corporations', Recourse to Arbitration by the United States under Article 22.6 of the DSU and Article 4.11 of the SCM Agreement*, WT/DS108/ARB, adopted 30 Aug. 2002, at para. 56; see also WTO Panel Report, *United States – Subsidies on Upland Cotton,* WT/DS267/R, adopted 8 Sep. 2004, at paras 1086 and 1292.

enterprise and which are given merely to provide time for the development of long-term solutions and to avoid acute social problems.'[191]

Accordingly, a differentiation between 'industry' and 'enterprises', on the one hand, and between non-recurrent one-time measures for exceptional situations and long-term support, on the other hand, is necessary and may provide for some leeway for governmental arguments in favour of subsidizing instruments. The conceptual distinction between 'industry' and 'enterprises' recurs in different articles of the SCM Agreement, such as Article 2.1 regarding the subsidy's specificity. Furthermore, Article 16.1 of the SCM Agreement defines the term 'domestic industry:'

> as referring to the domestic producers as a whole of the like products or to those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products, except that when products are related to the exporters or importers or are themselves importers of the allegedly subsidized product or a like product from other countries, the term "domestic industry" may be interpreted as referring to the rest of the producers.[192]

Generally speaking, however, there does not exist any rigorous definition in international texts; some guidance could be deduced from application of the simple view of 'distortion', standing at the core of the rationale for subsidies' regulations.[193] Furthermore, from a literal approach, 'industry' can be interpreted as the more extensive term, consisting of different individual enterprises.

As a consequence, the compatibility of governmental measures not least depends on whether the whole automobile industry is supported or whether the state measures concentrate on individual enterprises. In the former case, a serious prejudice is deemed to exist from the outset. In the latter case, the SCM Agreement does not prohibit one-time measures to prevent the worst. Such an interpretation deriving from Article 6.1 of the SCM Agreement may also influence the perception of the rest of the Agreement and could thus lead to a milder evaluation of the effects of state support in terms of Article 6.3. However, precaution is appropriate according to the terminology used in Article 6.2 of the SCM Agreement, which clearly requires an examination of both Article 6.1 and Article 6.3 as cumulative criteria necessary for an assessment of serious prejudice.

5.4.3.2. *Justification*

The last step in the examination of whether 'serious prejudice' prevails in principle is the assessment of circumstances referred to in Article 6.7 of the SCM Agreement. Indeed, a justification on grounds of 'force majeure' could seem to provide for a hinging point in this context at first glance. However, according to a systematical reading, it would probably be difficult to list the man-made economic crisis in line with 'natural disasters, strikes and transport disruptions' according to Article 6.7(c) of the Agreement. Furthermore, in

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[191] Article 6.1(c) of the SCM Agreement, second part of the sentence.

[192] Reference to Art. 16 for the interpretation of the term 'industry' in Art. 2.1 of the SCM Agreement was, however, rejected by the Panel in the WTO Panel Report, *US-Softwood Lumber*, above n. 130, at para. 184. See also Luengo Hernández de Madrid, above n. 99, at 132–137 with further references.

[193] Benitah, above n. 99, at 275–279.

light of the global impact of the crisis and the resulting measures adopted worldwide, a supporting state could take the view that a possible complaining member is involved in similar protective measures, resulting in the fact that serious prejudice is not caused in terms of the circumstances listed in Article 6.7 of the SCM Agreement. According to the general principles applicable regarding the burden of proof in WTO dispute settlements, which comply with the generally accepted rule of evidence in civil law, common law, and most national jurisdictions, it is required that the party complaining or defending asserts the affirmative of a particular claim or defence.[194] As a consequence, the supporting state would have to defend itself by proving that the complaining party itself was adopting similarly subsidizing measures.

Arguments in favour of the various governmental measures bolstering research and 'smart' innovation in the fields of low-carbon markets, clean technologies, and energy efficiency in general could be derived from a glance at the no longer applicable Articles 8 and 9 of the SCM Agreement on non-actionable subsidies. Article 8.2(a) classifies assistance for research activities conducted by firms or by higher education or research establishments as non-actionable if the assistance covers no more than 75% of the costs of industrial research and 50% of the costs of pre-competitive development activity, respectively, and provided that such assistance is limited to specific costs.[195] Furthermore, Article 8.2(c) addresses 'assistance to promote adaptation of existing facilities to new environmental requirements imposed by law and/or regulations which result in greater constraints and financial burden on firms'. Such support is apt to justify a corresponding subsidy provided that it complies with four cumulative criteria, namely, that the assistance:

> (i) is a one-time non-recurring measure; and (ii) is limited to 20% of the cost of adaptation; and (iii) does not cover the cost of replacing and operating the assisted investment, which must be fully borne by firms; and (iv) is directly linked to and proportionate to a firm's planned reduction of nuisances and pollution and does not cover any manufacturing cost savings which may be achieved; and (iv) is available to all firms which can adopt the new equipment and/or production processes.

Sustainment helping to prevent environmental degradation can also be interpreted as a response to already existing imperfections of market signals where environmental costs are not considered as costs in the balance sheet and thus the products' prices.

Since the legal situation is not perfectly clear, due to the fact that the members of the Agreement were not willing to extend the provisions on non-actionable subsidies according to Article 31 of the SCM Agreement and dispute settlement has not provided much case law regarding these provisions,[196] a definitive assessment of whether state incentives in favour of green developments are compatible under WTO law is

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[194] See, e.g., WTO Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, adopted 25 Apr. 1997, at 14–17.

[195] For example, costs of personnel, costs of instruments, costs of consultancy, additional overhead costs, or costs of materials, supplies, etc.

[196] At least in WTO Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft, Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/RW, adopted 9 May 2000, at para. 5.24, by assessing whether a de facto export contingency existed in respect of the Canadian regional aircraft industry support, the Panel referred to ns 28 and 29 to former Art. 8.2(a) of the SCM Agreement for interpreting whether the fact that the results of a project may in the future be useful in the development of new products or their improvement would render a project 'near-market'.

not possible. Although bringing a case to the WTO based on environmental measures could cause political concerns, the nature of these types of justified subsidies should not be overestimated.[197] However, a margin for argumentation exists according to which a one-time, non-recurring supportive measure, complying with the cumulative criteria listed in Article 8.2(c), would not amount to a breach of the SCM Agreement.

5.5. Concluding remarks

As a general rule, subsidies shall be notified to the contracting parties according to Part VII and Article 25 of the SCM Agreement and Article XVI:1 of GATT 1994. Furthermore, if the granting of financial contributions amounts to adverse effects on the interests of other parties to the SCM Agreement, consisting in an injury or serious prejudice to their domestic industry, the implementation of a dispute resolution process cannot be excluded.[198] However, due to the substantial and widespread impacts that the economic crisis had on the real economy of various countries, it is rather implausible that consultation procedures would be filed in the very near future, not least in view of possible justifications under Article 6.7 of the SCM Agreement. Furthermore, in view of the auto industry's characterization by numerous cross-ownerships among companies, countervailing duty cases are also improbable. Such findings have lead to concerns that the auto industry could remove itself from the WTO regime, thus weakening the world trade system.

Additionally, according to Article VI of GATT 1994 and Part V of the SCM Agreement, countervailing duties may generally be imposed on the products from the subsidizing country, pursuant to the initiation of investigations to determine the existence, degree, and effect of any alleged subsidy according to Article 11 of the SCM Agreement. The term 'countervailing duty' is defined as meaning 'a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandize, as provided for in paragraph 3 of Article VI of GATT 1994'. Countervailing measures are thus implemented by the states as a reaction to adverse effects stemming from governmental interventions; thereby, other actors affected by the subsidized products, such as producers and the final consumers, are not taken into account explicitly beyond their standing within a state's national economy.[199] As a reaction to alleged adverse effects, such countervailing subsidies amount to further governmental interference with the market mechanisms and are thus subjected to particular provisions set out in Part V of the SCM Agreement.

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[197] See also Luengo Hernández de Madrid, above n. 99, at 161/162; Horlick/Clarke, above n. 99, at 28; Brunel & Hufbauer, above n.16, at 8, 10.

[198] According to Art. 7 of the SCM Agreement, any member having reason to believe that a subsidy amounts to adverse effects and is thus actionable under the Agreement may request consultations with the other (subsidizing) member. This also corresponds with Art. XVI GATT. If the consultations do not result in a mutually agreed solution within sixty days, any party to the consultations may refer the matter to the Dispute Settlement Body (DSB) for the establishment of a panel; panel reports may be appealed and thus subjected to the Appellate Body proceedings. According to the reference provided in Art. 30 of the SCM Agreement, Arts XXII and XXIII of GATT 1994 apply to consultations and the settlement of disputes.

[199] On this note see Benitah, above n. 99, at 98–101.

According to the outline given above,[200] the substantial support of the automobile industry by nation states may amount to a potential and specific subsidy according to the WTO/GATT legal framework. However, the financial contributions provided for sustaining a real economy market sector are not prohibited as such under international trade regulations; moreover, their treatment according to the traffic light approach adopted by the SCM Agreement depends on their individual embodiment and the context in which they are applied in. As a consequence, the classification of a financial benefit as a *prohibited* subsidy according to Part II of the SCM Agreement can be prevented rather easily by a supporting state. Nevertheless, the qualification of the governmental support as amounting to *actionable* subsidies in the long term provides for further challenges. As outlined above,[201] several lines of argumentation exist in an individual case to either argument in favour of a subsidies' actionability or not.

As a general rule and guiding principle for ascertaining a definition of actionable subsidies, the conceptualization of the '*distortions*' in question needs to be considered for an assessment of a subsidy. The subsidization of the automobile sectors may have an effect on the prices of cars benefiting from governmentally supported production processes, thus generally enabling the supported car producers to reduce market prices. The apprehension is brought forward that, under such circumstances, the market position of automobile enterprises that do not receive corresponding funding is threatened. A traditional view perceives subsidies as a practice distorting the natural comparative advantage between trading countries, due to the fact that they give wrong signals regarding the allocation of resources. Overproduction of the subsidized goods, stemming from distorted production costs, for example, is then linked to an underproduction of more socially valued goods, leading to a welfare loss for the world economy, 'insofar as the subsidized goods prevent the importation and thus the production of similar goods produced in a more efficient way in other countries'.[202]

However, it is important to note that interferences with the market processes in national economies do not necessarily entail a disturbance of international economical relations:

> [N]ot just any 'distortion' should suffice for the international system to take action. In some sense, every governmental action that impinges on the economy creates a 'distortion'. (…) However, it is a legitimate choice for a national sovereign to accept lower economic welfare in order to promote certain societal and governmental objectives (such as redistribution of income, or support for the handicapped). As long as the government's action are taken in such a way that the costs are borne only by that society, it seems inappropriate for other nations in the world to complain.[203]

The privileged treatment under the formerly existing Article 8.2(a) and 8.2(c) of the SCM Agreement of research and development subsidies and subsidies provided as assistance to promote adaptation to new environmental requirements, was fully coherent

[200] See 5.1/5.2.
[201] See 5.4.
[202] Benitah, above n. 99, at 252.
[203] Jackson, above n. 90, at 298–299. See also the examples for such a 'sophisticated view of distortions' provided by Benitah, above n. 99, at 254–256; see also Grave, above n. 99, at 130–133 on the function of the subsidy concept and at 258 et seq.

with the logic of taking into account possible positive external effects that compensate comparative advantage 'distortions'.[204] However, it is obvious that considering both positive and negative external effects of subsidies in the calculation of 'net countervailable subsidies' would amount to a rather insurmountable task for any legal system.[205]

In sum, although the concept of 'distortion' is an essential guide for interpreting subsidies and measures implemented in their response, the various meanings of 'distortion' and the manifold implementations as well as the fact that no exact definition is provided on an international level, lead to a situation in which it is impossible to foresee the actual application of such guidelines neither by the national authorities nor on an international level.[206] As a consequence, an assessment on a case-by-case basis is crucial.

6. Outlook

At present, it seems to be too early to assess the actual trade effects the governmental measures will have, since their announcements continue and adaptations to the altering situations proceed. Despite such a caveat, it can be concluded that it is commonly acknowledged – not least according to economic theories on free trade – that governments do have a role to play in the free markets and may even possess particular responsibilities to intervene in certain constellations. Therefore, governmental support of particular real economy sectors can be in compliance with the WTO/GATT legal frameworks as long as their provisions and principles are respected; governments thus possess considerable leeway within international trade law regarding the extent of their participation in the free markets. In a nutshell and for the present contribution, it can be inferred that legality and illegality of subsidies are dependent on their individual arrangements and the actual contexts they are applied in.

Notwithstanding such a legal assessment, these measures may nevertheless be in breach of spirit and purpose of free trade theories. From an economic point of view, state aid may be perceived as preventing necessary market adaptations to new situations. Seen from this angle, the collapse would provide for a valuable opportunity to facilitate structural reform, which may even include the necessity to produce less cars, for example. Arguably, governmental sector support should thereby be confined to sectors that are of systemic importance to the functioning of the wider economy.[207]

Corresponding to the finding that free trade theory and the applicable international legal frameworks are not necessarily congruent, warnings against protectionism and against the risks that protectionist measures may entail for the worldwide economic situation have been repeated. At the G20 conference, the leading industrial and emerging

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[204] See Benitah, above n. 99, at 265–267, listing traditional examples for activities with positive effects such as education, vaccination, and public transportation. Their subsidization should be admitted in order to avoid their underproduction relative to what society really desires. Furthermore, e.g. a subsidy helping to prevent environmental degradation can be interpreted as a response to already existing imperfections of market signals due to the fact that environmental costs are often ignored in price calculations.

[205] Benitah, above n. 99, at 273–275.

[206] Benitah, above n. 99, at 280.

[207] OECD Report, Going for Growth, above n. 58, at 20, 24–25.

countries verbosely expressed their concerns on increased trade barriers and their willingness to come to an agreement in the ongoing Doha Rounds of negotiations.[208] According to different international studies, however, seventeen of the twenty states themselves introduced barriers to trade in light of the ongoing economic crisis;[209] the analysis 'On the financial and economic crisis and trade-related developments' undertaken by the WTO at the beginning of April 2009 gives an impressive overview on spreading protectionist measures.[210]

However, the different fora concerned with the current crisis are not in the position of preventing further interventions by other means than by trying to convince their Member States to adhere to the principles of free markets. Additionally, the WTO has assumed a monitoring function under the auspices of the Trade Policy Review Body (TPRB), which is held to discuss on a regular basis the most recent trade-related developments and provide corresponding reports. The WTO has furthermore established a task force within its Secretariat with an advisory role regarding the trade implications of the economic crisis. Effective monitoring is carried out at regular intervals and needs to be based on accurate information; the WTO has to rely on its members and their notifications of the measures taken.[211] Reliable information is a first step towards enabling concerted action on an international level for securing free markets and improving the coordination of national and international responses.

The specific focus on the market branch of the automotive industry – an economic branch of importance primarily in industrialized countries – shall not cloud a more holistic view of the present crisis situation, which has particular impacts for the most vulnerable participants on the global markets. Moreover, it provides for an example of the challenges implicated by governmental support of the real economy. A particular threat of developing countries' global trade shares would risk to call into question one of the main factors legitimizing the current multilateral trading system.[212] Furthermore, newest estimates of the WTO-Secretariat expect a decrease in world trade for 2009 of about 9%.[213] The strengthened and liberalized market access envisaged with the conclusion of the Doha negotiations itself is estimated to stimulate the economy with approximately USD 150 billion. It is in light of such considerations that the WTO reiterates and aims at the negotiations' positive outcome. Besides officially supporting this endeavour, WTO Member States could take decisive and perhaps more credible steps themselves by no longer taking advantage of the legal gray areas inherent in the WTO framework.

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[208] See above n. 11.

[209] See E. Gamberoni & R. Newfarmer, 'Trade Protection: Incipient but Worrisome Trends', Trade Notes Number 37, International Trade Department: World Bank, 2 Mar. 2009, <www.worldbank.org/trade> (visited 23 Jun. 2009).

[210] See second WTO Report to the TPRB from the Director-General on the Financial and Economic Crisis and Trade-Related Developments, 20 Apr. 2009, WTO Doc. WT/TRP/OV/W1. See also third Report on the Financial and Economic Crisis and Trade-Related Developments, above n. 57.

[211] First Report to the TPRB on the Financial and Economic Crisis and Trade-Related Developments, above n. 14, at para. 6.

[212] Cottier, above n. 36, at 3.

[213] See the WTO 2009 Press Release, World Trade 2008, Prospects for 2009, <www.wto.org/english/news_e/pres09_e/pr554_e.htm> (visited 23 Jun. 2009).