

CANADA - IMPOSITION OF COUNTERVAILING DUTIES ON  
IMPORTS OF MANUFACTURING BEEF FROM THE EEC

*Report by the Panel*  
(SCM/85)

I. Introduction

1.1 In a communication dated 10 October 1986, which was circulated in document SCM/77, the EEC requested the Committee on Subsidies and Countervailing Measures ("the Committee") to establish a panel to examine a dispute between the EEC and Canada regarding the standing of the petitioners and the definition of industry in the countervailing duty proceedings brought against EEC exports of boneless manufacturing beef to Canada. This matter had previously been referred by the EEC to the Committee (SCM/75) under the consultation and conciliation provisions of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade ("the Code") but it had not been possible for the Committee to resolve the matter.

1.2 At its meeting of 29 October 1986, the Committee agreed to establish a panel and authorized the Chairman to decide, in consultation with the parties to the dispute on the final wording of the terms of reference of the Panel. The Committee also authorized the Chairman to decide, after securing the agreement of the signatories concerned, on the composition of the Panel (SCM/M/32, paragraphs 183-185).

1.3 At the meeting of the Committee on 3 June 1987 the Chairman informed the Committee that the terms of reference of the Panel were as follows (SCM/M/34, paragraph 104):

"To review the matter referred to the committee by the European Community in SCM/75 relating to the standing of the petitioners and the definition of industry employed by the Canadian authorities in the recently concluded countervailing duty case against Community exports of boneless manufacturing beef to Canada and, in the light of the facts of the matter, present to the Committee its findings concerning the rights and obligations of the signatories party to the dispute under the General Agreement as interpreted and applied by the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade."

At the same meeting the Chairman informed the Committee that, after securing the agreement of the parties concerned, he had decided on the following composition of the Panel (SCM/M/34, paragraph 125):

Chairman: Mr. Carl Henrik von Platen  
Members: Mr. Robert E. Hudec  
Mr. Adin Talbar

1.4 The Panel met with the two parties on 15 May and 29 June 1987. In addition, the Panel met on 14 May, 30 June, 15, 16 and 17 July 1987 and 21 and 22 September 1987. On 22 September 1987 the Panel submitted its conclusions to the parties.

II. Factual aspects

2.1 On 18 October 1985, the Deputy Minister of Revenue Canada (Customs and Excise), following consultations with the EEC as provided for in the Code, initiated an investigation under Section 31 of the Special Import Measures Act (SIMA) based on a complaint received from the Canadian Cattlemen's Association (CCA) regarding the alleged injurious subsidization of boneless manufacturing beef

exported to Canada from the EEC. On 26 February 1986 the Deputy Minister accepted an undertaking from the EEC to limit the annual quantity of the subject goods exported to Canada to 10,668 tonnes, and the investigation was suspended. The undertaking was subsequently terminated as a result of an objection by the complainant, and the investigation was resumed on 27 March 1986. On that day a preliminary determination of subsidization was made and the complaint was then referred to the Canadian Import Tribunal (CIT) for a determination on the issue of material injury.

2.2 In the course of its enquiry the CIT considered the legal issue of whether the petitioners, who are producers and feeders of live cattle, can be considered part of the domestic industry producing boneless manufacturing beef and thus have standing to complain and to advance a case of material injury to that industry. The CIT concluded that the CCA could be considered part of the relevant domestic industry. In its Statement of Reasons, the CIT indicated that the production of manufacturing beef in Canada was a continuous sequential process commencing with the live cattle and ending with the boxed grinding beef; that there was a high degree of functional dedication and economic dependence in this sequential process; that no one disputed that the primary purpose of raising beef cattle was to produce beef, and that grinding beef was merely one of the product forms produced by the cattlemen. It also noted that others engaged in the production of manufacturing beef, i.e. the slaughterers and boners, the dairy industry and the packing houses contributed in varying degree to the goods in question, but said it was not persuaded that the various elements in the chain should be isolated into separate industries.

2.3 A final determination of subsidization was made on 12 June 1986 by the Deputy Minister. On 25 July 1986 the CIT made its final determination on the issue of material injury. The CIT found that some price suppression had taken place in association with the presence of the subsidized beef in the Canadian market, but it was not persuaded that such a suppression could be considered material injury, given the other factors influencing prices in the North American market. The CIT did, however, find a threat of material injury. It considered that in the absence of countervailing duties, exports from the EEC of the subject goods would be resumed in substantial volume, would likely divert Canadian beef into the US market and would thereby provoke a possible retaliatory action by the United States against Canadian exports of beef and cattle to that country. Two initiatives on behalf of the US interests had been noted in this respect, one in the form of a communication from the National Cattlemen's Association of the United States indicating an intention to seek government action to deal with "displaced" exports to the United States, and the other in the form of bills submitted in the US Congress calling for investigation of Canadian exports as "back door" entries of EEC products. In accordance with these final determinations of subsidization and threat of material injury, countervailing duties were imposed on imports of manufacturing beef from the EEC.

2.4 In Canada there are three distinct sectors which form the primary source of manufacturing beef: the cow-calf sector, the feedlot sector and the dairy sector. The principal product of the cow-calf sector are calves which are sold to the feedlot sector. The cows and bulls used to produce these young animals are marketed (culled from the herd) when they become too old or unproductive or when a producer wishes to reduce production. The culled cattle are turned into manufacturing beef. The principal product of the feedlot sector is finished cattle (i.e. calves which have been bought at a typical weight of 500 lbs. and fed to approximately 1,200 lbs.) which are slaughtered to produce grades of beef higher than manufacturing beef. Those parts of the carcass not suitable for high-grade beef (some 17-20 per cent) are used as manufacturing beef. In the dairy sector cows culled from the dairy herds are sold to provide the third source of manufacturing beef. The proportion of manufacturing beef originating from these three sectors is as follows: cow-calf, 36.5 per cent; feedlot, 46.5 per cent; and dairy, 17 per cent. The complainant in the countervailing duty case, the CCA, represented producers in the cow-calf and feedlot sectors. Representatives of the dairy sector were not parties to the proceedings.

2.5 According to the figures presented by Canada, when cows and bulls culled by cow-calf operators and dairy farmers are slaughtered for manufacturing beef, approximately 85 per cent of the usable

carcass is manufacturing grade beef and 15 per cent is high grade beef. In the case of feedlot operators, 17 to 20 per cent of the usable carcass of feedlot steers and heifers enter into the production of manufacturing beef. The sale of cows and bulls for manufacturing beef accounts for approximately 20-25 per cent of income earned by cow-calf operators, and for the dairy farmer it accounts for 10-15 per cent of income. There are no precise data as to what part of income of a feedlot operator is derived from sales of manufacturing beef. The Canadian delegation estimated that the return was less than the weight percentage going into this production (i.e. less than 17-20 per cent). At the wholesale level, the value of the live animal used to produce manufacturing beef constitutes 66 per cent of the total value of manufacturing beef sold.

2.6 In Canada there is little vertical integration between suppliers of cattle and the firms which perform slaughterhouse and boning operations. Processing operations are sometimes performed by integrated firms while in other cases the slaughtering and boning operations are performed by separate firms. The Canadian firms engaged in processing operations were not parties to the countervailing duty proceeding and took no position on the question of material injury.

2.7 The Canadian delegation supplied the following information pertaining to the relationship between imports of boneless manufacturing beef and prices in the cattle-raising sector: According to a staff report prepared for the CIT in the present case, during the years 1983-1986 there was an 85 per cent correlation between the spot price of boneless manufacturing beef in Toronto and the price of manufacturing-grade cows in Toronto. In general, the supply of manufacturing-grade animals tends to be price inelastic. The number of culls removed from herds is determined in part by the need to remove unproductive animals in order to maintain an efficient production system. There are over 100,000 cow/calf producers in Canada, and there is no government regulation of supply. Historically, due to relatively unrestricted trade between the two markets, price movements in Canada have been strongly influenced by the prices for similar quality products in the United States. In such circumstances, when the Canadian price for any grade of cattle fell below the price in nearby US markets by more than the cost of moving the product (duty, transportation, brokerage) Canadian cattle could be sold in those US markets, providing a floor for Canadian prices.

### III. Main arguments

3.1 In the view of the EEC the decision of the Canadian authorities to initiate an investigation in this case and the decision to consider the CCA to be producers of the like product for the purposes of material injury findings constituted violations of Canada's obligations under Articles 2:1 and 6:5 of the Code.

3.2 The EEC considered that the essence of the dispute could be reduced to one question: can the CCA be considered under the Code to be a domestic producer of the like product. The answer to that question would be determinative as to whether: (i) the CCA had standing to file a petition (Article 2:1 of the Code) and (ii) the CCA could be considered to be part of the domestic industry for the purposes of injury determination (Article 6:5 of the Code).

3.3 The EEC view was that there was no dispute that boneless manufacturing beef, the product exported from the EEC, was produced in Canada, and that this product constituted the like product. The question was who produced it. The EEC had no difficulty with the notion that there were a series of production processes involved in the production of beef and that the cattle producers, feedlot operators, and dairy producers produced the input product from which manufacturing beef eventually emerged. However, that input product - live beef animals - could not be described as a "like product" to boneless manufacturing beef because it could not be said to have physical characteristics identical to those of boneless manufacturing beef. At least two further stages of industrial processing were required.

3.4 The EEC noted that Article 6:5 of the Code defined domestic industry as domestic producers of the like product. The EEC argued that the use of the word "shall" made this definition mandatory. The term "producer" clearly referred only to the industry which produced the like product itself - not the industry which produced an input product. The concept of "domestic industry", as defined in Article 6:5 also determined the interpretation of the term "industry affected" in Article 2:1. This precise definition did not allow for a creative interpretation which would upset the delicate balance of rights and obligations which was the result of laborious negotiations during the Tokyo Round.

3.5 The EEC drew attention to an earlier Panel Report (United States -Definition of Industry Concerning Wine and Grape Products - SCM/71) in which, it argued, a similar interpretation of the term "producer" had been accepted. The EEC noted that the panel report had not yet been adopted by the Committee on Subsidies and Countervailing Measures, but argued that the obstacle to approval had been merely procedural and did not detract from the relevance of the panel's conclusions.

3.6 The EEC further argued that this strict interpretation of the term "producer" was confirmed by the wording of Article 6:6. The purpose of Article 6:6 was to lay down precise rules on how to assess the effects of subsidized imports. The normal rule was that different products produced by the same enterprise had to be examined separately. The only derogation from this rule was in cases where there were no separate accounting systems for the different products produced. Applying this principle to the type of vertical production process involved in this case, the EEC argued that, where there was no vertical integration, or where separate accounting systems existed irrespective of organizational structure, processing operations had to be regarded as separate industries. Furthermore the EC emphasized that the very fact that it was felt necessary in Article 6:6 to mandate that when the domestic production of the like product had no separate identity then the effects of the subsidized imports had to be assessed in relation to the narrowest group or range of products, showed that the intent could not have been to permit a wide interpretation in the situation where a separate production process was identifiable and where the industry was not vertically integrated.

3.7 The EEC view was that, in the production of manufacturing beef in Canada, the processing industry could be separately identified in terms of the production process, producers' realization and profits. Since this was the case, the Code mandated that the effects of the subsidized imports had to be assessed in relation to this industry. It followed, therefore, that an assessment of the allegedly injurious effects of subsidization on the cattle producers, which neither produced the like product nor were integrated in the industry which did produce it, could not be consistent with Article 6:5 and 6:6 of the Code.

3.8 The EEC also recalled that Article 6:5 of the Code derived from Article VI of the GATT which itself constituted an exception to the general principles of Article I and therefore had to be subject to a narrow interpretation. Since, by their very nature, anti-dumping and countervailing duties were discriminatory in nature, a precise and tightly drawn definition of the domestic industry was indispensable for assessing material injury. The EC also noted that the Canadian decision to include cattle producers as part of the industry producing boneless manufacturing beef did not accord with past decisions of the CIT (or its predecessor body) in which a separation had been made between processors and producers of the raw agricultural product. Finally the EC argued that if the Canadian authorities interpreted the concept of "material injury to the production of like goods" in the SIMA to be synonymous with material injury to producers engaged in the production of like goods as adopted in the case in dispute, then these provisions of Canadian law could not be considered to be in conformity with the Code which restricted the assessment of injury to domestic producers of the like products.

3.9 Canada agreed that the central issue for the Panel to examine was the definition of industry for purposes of determining standing and assessing material injury. Canada noted that while Article 6:5 of the Code defined the term "industry" as domestic producers of the like product, there was no strict

definition of the term "producers". In this regard Canada argued that, in contrast to the EEC'S interpretation, Article 6:6 of the Code did not clarify the definition of industry but rather stated that the effects of imports were to be assessed in terms of the production of the like product, in this case, boneless manufacturing beef. Article 6:6 did not provide guidance in identifying the "producers" of the like product. It did however, provide guidance for identifying the like product where production of the latter could not be separately identified from the production of other products. Canada also argued that the Code offered some flexibility to take account of economic or market realities. For example, the Code permitted, under certain circumstances, the segmentation of an industry into regional components so as not to deny relief to producers in specific regions from injurious foreign subsidization, even though a major portion of the total domestic industry was not being injured (Article 6:7). The Code also allowed for a broader definition of industry to take account of integration of markets in a customs union, by treating the industry within the entire customs union as one industry (Article 6:9).

3.10 Canada argued that GATT jurisprudence and the drafting history regarding the concept of definition of industry demonstrated that, for purposes of assessing material injury, there was some flexibility regarding the definition of industry in horizontal terms based on the specific economic circumstances surrounding the production of the particular product in question. With respect to GATT jurisprudence, Canada noted that a Panel regarding the dumping of electrical transformers (New Zealand -Imports of Electrical Transformers from Finland - L/5814), following an examination of economic circumstances, rejected an effort to have the definition of industry narrowed to particular production lines, even though the products concerned were capable of separate identification. The Panel concluded that "it was the overall state of the New Zealand transformer industry" which must provide the basis for assessing material injury. Canada argued that the definition of industry was thus sufficiently flexible to allow for the grouping of heterogeneous products (i.e. electrical transformers which, according to size or power rating, differed in design, manufacturing technique and marketing), resulting from horizontally separately identifiable production processes, into a single industry. Canada considered that the concept of industry had to be interpreted in a similarly flexible manner in the present and recognize the special vertical relationships involved in the production of manufacturing beef in Canada.

3.11 Canada drew attention to the drafting history of the original Anti-Dumping Code, from which the Subsidies and Countervailing Measures Code borrowed the definition of industry (GATT Anti-Dumping Checklist: comments by governments on Items I-V and IX-XIII, (TN.64/NTB/W/12/Add. 1-9, 13 July 1966), as well as Draft International Code on Anti-Dumping Procedure and Practice: Note by the United Kingdom Delegation, Spec(65)86, 7 October 1965) and argued that it provided further evidence that there was no single approach to defining an industry and of the importance of considering the specific economic circumstances affecting the production of the like product. In the Canadian opinion there had been a general view that the definition of industry had to be sufficiently flexible to include those producers that could potentially suffer material injury, but at the same time, rigid enough to exclude those that were not. It argued that while the drafting history revealed a concern regarding the definition of industry in horizontal terms, the principle was one of ensuring protection to those suffering material injury, based on an examination of the economic realities of each case. The task was to define the range of products so that it was not too broad as to effectively dilute the remedies for injurious subsidization or dumping, or too narrow as to provide undue protection to a particular segment of an industry. Canada considered that this principle logically applied to the vertical relationships that existed within the Canadian manufacturing beef industry.

3.12 Canada agreed that the process of identifying the domestic industry was generally straightforward as the industry producing the like product could be easily identified. However, in some cases, this simple and straightforward approach did not necessarily make sense. This was particularly true of industries characterized by the following: (i) a continuous sequential process of production involving the use of only one raw material input which, by undergoing relatively little processing prior to

becoming an end-product, accounted for a substantial proportion of the value of the end-product; (ii) an input which was functionally dedicated to the manufacture of only one end-product and which had no economically viable alternative uses; (iii) a situation of economic interdependence in which end-product producers were able to pass back to input producers a decrease in the price of the end-product resulting from competition from subsidized imports.

3.13 In the Canadian opinion the production process in the boneless manufacturing beef industry in Canada satisfied these three conditions. There was a single continuous line of production which started with one raw material (the live animal or parts thereof) and yielded only one significant end product (boneless manufacturing beef) . Furthermore, there was no other economically viable use for culled cattle from the cow-calf and dairy sector or for the manufacturing beef derived from the feedlot sector. Moreover, at the wholesale level, the value of the input, i.e. the live animal used to produce manufacturing beef constituted 66 per cent of the value of the end product. Finally, most of the injury associated with the importation of boneless manufacturing beef was not felt by the slaughterhouses, but was passed backward to the producers of the livestock in the form of lower bid prices. The primary factor affecting a slaughterhouse's bid price for cows destined for the production of boneless manufacturing beef was the price for said beef. According to a staff report prepared for the CIT, there was an 85 per cent correlation between the price of manufacturing beef and the price of manufacturing grade cows.

3.14 Canada considered that, cast in terms of economic theory, a cattle producer's supply curve was effectively inelastic. In the short run, he was unable to control the supply of cattle going to market. The supply of cattle was determined by factors unrelated to the price of beef or cattle, including grade, weight, age and condition of the animal, regional feed supplies, etc. Cattle producers also faced a perfectly elastic demand for their animals. If higher prices were demanded than those determined in the market, they would be unable to sell their animals. In other words they were price-takers. Processors in effect acted as intermediaries in a market where demand was determined at the consumer level and supply, by the number of cattle available at the farm level. These characteristics meant that processors had the ability to pass back injurious effects of imports of subsidized beef to Canadian cattle producers. Cattle producers had to absorb almost all the injury as they could not adjust the quantities they supplied to market.

3.15 Canada concluded that the above-mentioned factors necessitated including livestock producers in the industry that produced manufacturing beef in Canada. It considered that to deny protection to livestock producers would be to deny protection to that segment of the industry that was the most susceptible to injury caused by imports of subsidized manufacturing beef. This would be at variance with the principle of ensuring protection from injurious foreign subsidization via appropriate countervailing duty measures. The fact that the processors did not join the livestock producers in their complaint was explained by the former's ability to pass back any price decrease resulting from imports of subsidized manufacturing beef to the latter.

3.16 Canada rejected the EEC argument that the Panel Report in the Wine case was relevant to the definition of industry in this case. Because the report had not been adopted, it had no standing and should not be considered. In addition, Canada argued, the production process involved in the Wine case was distinguishable from the production process for manufacturing beef involved in the present case. In this regard, it considered that: (1) while there was no other economically viable use for culled cattle or lower quality parts of high-grade cattle than to be processed into manufacturing beef, according to the United States International Trade Commission (USITC) only 42-55 per cent of wine grapes were used in the production of wine, there being other major markets for wine grapes (e.g. table grapes and raisins); (2) while the value of manufacturing beef produced by packers was not a great deal higher than that of live animals entering the production process, the contribution of wine grapes to the value of wine was considerably lower (an estimate of a comparable figure for Canadian production was 14 per cent); and

(3) while beef processors had the ability to pass back injurious effects of imports of subsidized beef to cattle producers, wine producers had limited ability to do so as wine grape producers have significant alternative markets for their output.

3.17 Regarding the question of whether the CCA represented "the domestic producers as a whole of the like products or those of them whose collective output of the products constitutes a major proportion of the total domestic production" as required by Article 6:5, Canada argued that the CCA represented some 55 per cent (0.83 x 0.66) of the relevant industry. Some 83 per cent of the manufacturing beef produced in Canada was sourced from cow-calf and feedlot operators represented by the CCA. Live animals constituted some 66 per cent of the wholesale value of the beef sold.

3.18 The EEC held the view that the three special factors identified in Canada's argument did not affect the definition of industry in Article 6:5 of the Code. The fact that boneless manufacturing beef emerged from a "continuous sequential" process of production was irrelevant to the question of whether the CCA produced the like product. No such test was incorporated in the Code. The only criterion for judging if a certain producer was part of the domestic industry was whether he produced the like product.

3.19 Regarding the test of "functional dedication" in general the EEC view was that such a test likewise had no basis in the Code. Many inputs - industrial as well as agricultural - were functionally dedicated to produce an output product (e.g. circuit boards for electronic products, mecadecks for video tape recorders, photoconductors for photocopiers). This did not, however, confer on the input product producers the right to complain about allegedly subsidized or dumped end products, nor for any injury to them to be taken into account when assessing injury to the producers of the end product.

3.20 The EEC considered that "economic interdependence" of the kind alleged by the Canadian authorities existed in many sectors, agricultural as well as industrial. Referring to the examples cited earlier, the EEC said that circuit board manufacturers supplying subassemblies to TV or office equipment manufacturers might be as much injured by subsidized imports of the end product as by subsidized imports of their own products. However, the Code did not rely on such arguments but instead restricted the definition of industry to producers of goods having the same characteristics as the imports concerned.

3.21 The EEC was of the view that the Panel decision in the Electrical Transformers case did not support the Canadian position with regard to the claimed flexibility of the definition of industry in the Code. The EEC considered that the Transformers Panel had defined the relevant industry to include all product lines of transformers made by the manufacturer because it had concluded that all the transformers in question were "like products". Moreover the Transformers Panel had in effect dealt with a case of "horizontal" integration of lines of production not, as in the case of dispute here, with a situation where the issue was whether producers of the raw agricultural products might be considered as part of the industry producing the end product ("vertical integration"). As there was no argument in the present case that live cattle and boneless manufacturing beef were like products, the EEC viewed the Transformers Panel decision as irrelevant to the current dispute. With regard to the argument advanced by Canada that the general preamble of the Code justified relief being made available to those producers adversely affected by the use of subsidies, the EEC maintained that the correct approach was to look at the operative part of the Code (Article 6:5). Only when this was not clear - which was not the case here - could some reliance be placed on the general statements of the preamble.

3.22 The EEC recognized that different views were possible on the question of Whether the Code's definition of industry was inequitable. On the other hand, the EEC argued that a broadening of the frontiers of the actual disciplines of the Code would open a Pandora's box and would lead to effects opposite to those desired by most if not all negotiators of the Code. In any case such broadening of the actual definitions was not a matter for unilateral interpretation but would require a rewriting of the Code

provisions. Irrespective of whether the existing provisions were perceived to be equitable or not, Code signatories should ensure that they were applied unless they were modified through multilateral negotiation.

3.23 The EEC further argued that, even if, for the sake of argument, the tests enunciated by Canada had had some legal basis in the Code, it was doubtful whether they had been properly applied by the Canadian authorities in this case. Boneless manufacturing beef was essentially a by-product resulting from economic activities whose principal aim was to produce other products for sale, a fact borne out by the proportion of income derived from boneless manufacturing beef by cattlemen. Viewing the entire economic process by which inputs were produced for transformation into boneless manufacturing beef it could not be said to involve either continuous production or functional dedication in the sense called for.

3.24 Canada rejected any allegation that it was arguing that manufacturing beef and live cattle were like products. It did not dispute that in a physical sense live cattle and beef were not identical, although the issue of what is a like product was not as clear as the EEC appeared to suggest. Nor was Canada arguing that input producers generally had the right to request countervailing duty action against imports of end-products. Canada argued that, given the particular economic relationship between Canadian cattle producers and beef processors and the particular nature of the Canadian manufacturing beef production process, Canadian cattle producers were necessarily part of the industry producing manufacturing beef. This determination was entirely appropriate given the fact that the Code did not provide precise guidance to identify the producers which constituted the industry and the fact that the drafting history of the definition of industry in the GATT and the Code indicated a great deal of concern regarding the need to consider the production process of each individual case, in particular, the need to ensure that the definition of industry corresponded to the reality of who bore the incidence of material injury. It rejected the EEC's contention that the Transformers Panel report was irrelevant to the present case and referred to its earlier argumentation that the flexibility applied in aggregating heterogeneous products resulting from horizontally separately identifiable production processes logically applied to the vertical relationships characteristic of the manufacturing beef industry in Canada. Canada also rejected the contention that the definition of industry applied in this particular case was somehow opening up a Pandora's box. It noted that the examples cited by the EEC during the proceedings attempting to show that the criteria applied by Canadian authorities would provide input producers with additional rights or that the relationship between cattle producers and beef processors pervaded industry generally, had, to the contrary, illustrated the special nature of the situation before the Panel.

3.25 Canada also rejected the EEC's contention to the effect that even if the criteria applied by Canadian authorities in defining the manufacturing beef industry in Canada had a legal basis in the GATT, the results were incorrect. Canada felt that the EEC was, in effect, arguing that the sources of manufacturing beef, i.e. culled cattle from the feedlot and dairy sectors as well as trimmings from fed cattle, were not functionally dedicated to the production of manufacturing beef, because their past uses were more important in economic terms. Canada argued that this was irrelevant for the purpose of defining the manufacturing beef industry in Canada. It noted that there was no other economically viable use for culled cattle and trimmings than to be turned into manufacturing beef and that the prior uses of the cattle were of little importance to this fact. It also noted that the income derived by cattle producers from sales to processors of manufacturing beef often determined the viability of cow-calf operations.

3.26 Canada furthermore considered that to reject, as did the EEC, the contention that cattlemen were part of the manufacturing beef industry would create a situation whereby levels of relief varied according to differences in industry structure between countries, or according to the evolution of industry structure over time, rather than according to the incidence of material injury. The net result of the EEC interpretation would be that livestock production in an integrated production process would benefit from the provisions of Article VI of the GATT with respect to imports of subsidized beef while

livestock production in a non-integrated production process would not. This would not only be inequitable but also inconsistent with one of the basic purposes of the Code enunciated in the Preamble, ensuring that relief is made available to those producers adversely affected by the use of subsidies.

#### IV. Submissions by third countries

##### (a) Australia

4.1 Australia believed that the decision on the standing of the CCA in the case under consideration was consistent with the spirit of the GATT and the Code. In its view it was the members of the CCA who produced the beef. Abattoirs simply put the production into a usable form. Abattoirs were highly mechanised establishments performing a necessary physical stage of the production function which traditionally could and did take place at the farm or village level. THE production process was, therefore, a continuous line that produced only one commercially significant end product, i.e. beef. Cow-calf operators could therefore be considered part of the industry which produced boneless beef. On the other hand, dairy producers who subsequently slaughtered or sold aged cows or cull heifers from which manufacturing beef was produced would be engaged in this activity as an incidental to the main commercial enterprise, i.e. dairy. As such there could be doubts as to whether the dairy producers could be considered a part of the industry for the purposes of the countervailing duty action against subsidized beef from the EEC. Australia saw support for this view in Ad Article XVI of the General Agreement, Section B, paragraph 2, which defined a primary product as "Any product of farm ... in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade." In Australia's view if manufactured beef was not a product of farm industry but was a manufactured product, it followed that the payment of any subsidy on export would be a breach of Article 9 of the Code. Australia submitted that the Panel should look closely at this question if it found itself unconvinced regarding the merits of the Canadian submission.

4.2 Australia pointed out that it was the over-riding objective of the Code to ensure that the use of subsidies did not adversely affect or prejudice the interests of any signatory. The use of countervailing measures was justified where the subsidized product was having or threatening to have a direct and prejudicial impact on the domestic industry. If subsidized beef from the EEC entered the Canadian market in large quantities, it was the Canadian cattle farmers who were hurt by the effect of subsidized imports on price formation in the market place and on sales opportunities for their cattle. Australia considered that it would be inequitable if countervailing duty action was not available to the Canadian cattle producers in this situation while the EEC used import quotas, minimum import prices and variable levies, which by their protective effect precluded the need for comparable countervailing action.

4.3 Australia maintained that its industry data substantiated the point that it was the cattlemen who took the ups and downs of the beef market. Industry data showed that the domestic saleyard price constituted at the present time about 60 per cent of the final beef price in Australia at the dock before loading for shipping overseas. However, abattoirs had fixed costs plus profit which would represent a variable depending on overall meat prices.

4.4 In regard to the EEC assertion that it was the packing companies that were the producers of boneless manufacturing beef, it was Australia's view that the packers constituted only part of the total production process. The cost of killing and transporting to the dock in Australia was presently only 40 per cent of the final cost of the beef at the dock. The price to farmers reflected market price and market process costs and therefore disturbance of the beef market was primarily prejudicial to the producers rather than the packers. Packers might actually gain from the supply of subsidized EEC beef by forcing down prices paid for domestic cattle while not suffering any reduction in the return on the processing end of the production cycle.

4.5 To illustrate its point Australia made the following observations on the definition of industry in the dispute between the USA and EEC over wine imports. Given that grape growing can be dedicated

to production for the dried vine fruit industry, for table grapes or for wine production and that these three functions may be undertaken by the same person, not involved in wine making, it is difficult to argue conclusively that grape growing as such is part of the wine industry. However, if the only type of grape is a wine producing grape, then it would be difficult to argue that the grape grower is not part of the wine industry as he received no return for his produce unless it is converted into wine and that return must reflect the value of wine and the cost of processing. A parallel exists between this latter example and the breed cattle industry, where the fundamental purpose for raising beef cattle is the production (and consumption) of bovine meat. Australia pointed out that in the present case, the Panel was considering a product where there was minimal transformation of the raw material, and then only sufficient as was customarily required to prepare it for marketing in substantial volume in international trade. As indicated by GATT International Meat Council data, only a small percentage of meat was actually traded internationally as live slaughter animals. The great bulk of bovine meat was traded as fresh, chilled or frozen beef and veal, with frozen being the major form.

(b) United States

4.6 The United States agreed with the Government of Canada's legal conclusion that under Article 6:5 of the Code producers of certain agricultural products could be treated as part of the industry producing a processed like product. The United States treated growers of a raw agricultural product as part of the industry producing a processed agricultural product when certain conditions were met. In this respect, the United States had considered: (i) the extent to which the raw product enters into a single continuous line of production resulting in the processed product and (ii) the degree of economic integration between the growers and the processors. These criteria were designed to identify situations where the activities of the growers were inextricably part of the production of the final like product. In such situations, it made little sense to say that the growers were not engaged in production of the like product. Their activity might take place at an earlier point in the production process, but they were no less engaged in production of the final like product than the processor who completed the manufacturing process.

4.7 In the United States' view, one of the fundamental purposes of the Code was to ensure that "relief is made available to producers adversely affected by the use of subsidies within an agreed international framework of rights and obligations." If the aim of the Code was to provide relief against the injurious effects of subsidized imports, it followed that the provisions of Article 6:5 should be read in a manner that accorded with economic reality. In this case the economic reality was that the activity of the growers was part of a chain of production that started with a raw product and ended with a single like product and it was often the cattle producer who suffered injury as a result of dumping or subsidization. If subsidized imports forced down domestic prices, the meatpacker often would pass along the injury by reducing the price that he paid for beef cattle. Thus, the impact of the subsidies came to rest with the cattle producer. This producer, moreover, had no alternative use for his beef cattle. They could only be sold for beef. He was in every sense of the word part of the beef industry and a victim of injurious subsidization.

4.8 As a further explanation of its position the United States delegation drew attention to relevant decisions of the USITC, dealing with legal issues similar to those involved in this case.

V. Findings and conclusions

5.1 The Panel agreed with both parties that the central issue to be decided was whether, both for the purpose of determining standing to complain under Article 2:1 of the Code and for assessing "injury" under Article 6 of the Code, the cattlemen and feedlot operators represented by the Canadian Cattlemen's Association (CCA) could be considered part of the relevant "domestic industry" within the meaning of Article 6:5 of the Code. The elements of that issue were also not in dispute. Article 6:5 defines the relevant "domestic industry" as "the domestic producers ... of the like products". The term

"like product" is defined in footnote 18 to Article 6:1 as:

a product which is identical, i.e. 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,

The Panel agreed with the parties that the "like product" in this case was manufacturing beef, fresh or frozen, and that live cattle produced by cattlemen and feedlot operators were a different product not within that definition. Consequently, the question whether cattlemen and feedlot operators could be considered part of the "domestic industry" turned on whether they could be considered "producers" of manufacturing beef.

5.2 The Panel began by examining the text of the applicable provisions. It noted that Article 6:5 did not contain a definition of the term "producers". It observed that, in common usage, one is normally considered the "producer" of only those goods one actually makes and sells; one who produces a new material is not normally regarded as a "producer" of the end-product.

5.3 The Panel noted that Article 6:6 expressed a principle that would support interpreting the term "producer" in accordance with its normal meaning. Article 6:6 defines more exactly the production process that is to be considered when assessing the effect of subsidized imports on "domestic producers ... of the like products." It states that the assessment shall be limited to the production process devoted to making the like product itself, except that, if the production process for that specific product cannot be separately analyzed, the assessment shall be made in terms of the production process for the narrowest group of products including the like product for which data are available. Article 6:6 thus indicates a preference for narrowing the analysis of injury to those production resources directly engaged in making the like product itself. Applied to a vertical production process involving several stages, this principle would indicate that the analysis should likewise be focused on the stage of production devoted to actually making the like product in question, as opposed to earlier stages devoted to producing inputs.

5.4 Under the normal meaning of "producer" indicated by the text of Article 6:5 and 6:6, the cattlemen represented by CCA could not be considered producers of manufacturing beef. The good they actually produced (cattle) was not itself the "like product", and their cattle-raising operations were clearly separate from the subsequent processing operations where cattle were made into manufacturing beef, virtually all of which were under different ownership.

5.5 The Panel then addressed the main argument made by Canada, supported by Australia and the United States, in favour of interpreting the term "producer" to include certain suppliers of inputs. As noted in paragraph 3.12 above, Canada proposed that input suppliers be considered "producers" of the end-product if their economic relationship to the end-product satisfied three criteria:

- (i) the end-product is produced by a continuous sequential process of production involving only one raw material input which undergoes relatively little processing and Which accounts for a substantial proportion of the value of the end-product;
- (ii) the raw material input is "functionally dedicated" to the production of only one end-product and has no economically viable alternative uses;
- (iii) the relationship involves a situation of economic interdependence in which the price impact of subsidized imports will generally be passed back to the input suppliers.

As the Panel understood the Canadian position, the three criteria were meant to identify situations in which all or most of the adverse economic impact from subsidized imports would be concentrated on the

raw material supplier. Canada argued that signatory governments had intended the Code to be interpreted in a sufficiently flexible manner to permit governments to grant protection to such suppliers.

5.6 In evaluating Canada's argument, the Panel examined the various legal sources which in its view had a bearing on the principles of interpretation embodied in the Code. The Panel first considered Canada's reference to the paragraph in the preamble to the Code stating that signatory governments desired "to ensure that ... relief is made available to producers adversely affected by the use of subsidies". The Panel appreciated the force of this objective, which would be implicit in any event. It noted, however, that the same paragraph of the preamble stated that governments also desired to ensure that "countervailing measures ... not unjustifiably impede international trade" and that relief to producers be made "within an agreed international framework of rights and obligations". These objectives express a recognition that the remedies provided by countervailing duty laws also impose burdens of expense and uncertainty that can impede legitimate international trade. In the Panel's judgement, the overall objective of the Code must be viewed as one of striking a balance between the injuries to be remedied and the injuries caused by providing such remedies. Thus, the fact that subsidies may be causing a particular injury does not by itself establish that the Code meant to provide a remedy for it.

5.7 The Panel then considered whether the express exception to the Code's definition of "domestic industry" in Article 6:7 indicated a policy of flexible interpretation in this area. Article 6:7 provided that, under certain conditions where separate regional markets could be said to exist, the relevant "domestic industry" might be limited to the producers in that region alone. Canada argued that Article 6:7 could be viewed as evidence of an intention on the part of signatory governments to accept a flexible definition of industry when out-of-the-ordinary conditions caused injuries to occur otherwise than as normally anticipated. The Panel considered, however, that the existence of Article 6:7 could also be interpreted to mean the opposite, i.e. that governments preferred to deal with out-of-the-ordinary situations by means of express exceptions in the text, and that the presence of an exception for regional industries but none for input suppliers meant that none was intended for input suppliers.

5.8 In weighing the evidence relating to the intent of signatory governments, the Panel attached particular importance to the negotiating history of the applicable Code provisions. In the Panel's view, this history revealed a general preference for legal standards employing objective criteria rather than criteria calling for application of economic judgement. This preference appeared to rest primarily on government concerns to limit the potentially burdensome effects of anti-dumping and countervailing duty proceedings, and in particular a concern that criteria calling for assessment of economic phenomena might provide an open-ended basis for initiating proceedings. The governments which drafted these provisions appeared willing to sacrifice a degree of economic precision in order to create legal standards which could be applied with greater certainty, and which would operate to terminate suspect complaints at the outset rather than requiring parties to go through the uncertainty and expense of a full investigation in every case.

5.9 The Panel found such a policy reflected in the requirement of standing to file complaints under Article 2:1. In the negotiation of the 1967 Anti-Dumping Code<sup>1</sup> from which the text of the current Article 2:1 provisions was drawn, governments agreed after considerable debate to require that complaints must normally be filed on behalf of the relevant industry as a whole, and not, as advocated by the United States<sup>2</sup> and Canada<sup>3</sup>, by any party which considered itself injured. The US and Canadian

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<sup>1</sup>Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (hereinafter referred to as Anti-Dumping Code of 1967) BISD 15S/24. Article 5:1 of the 1967 Code contains the text which now appears in Article 2:1 of the Code.

<sup>2</sup>TN.64/NTM/W/10/Add.3, p.7 (28 April 1966).

<sup>3</sup>TN.64/NTB/W/15 (21 February 1967).

view favoured giving every complainant a chance to prove its case. The opposing view, which prevailed, was expressed by the delegation of the United Kingdom:

The conditions governing the initiation and acceptance of applications for anti-dumping action determine to a large extent the number of anti-dumping cases which arise and the number which are eventually dismissed because full investigations show that action is not justified. In the view of the United Kingdom, therefore, it is of crucial importance that these conditions should be such as to reduce to the minimum the number of unnecessary anti-dumping investigations, and thereby prevent unjustifiable disruption of trade.<sup>1</sup>

When the provisions of the 1967 Anti-Dumping Code relating to standing were carried over into Article 2:1 of the Code in 1979, they were made even more restrictive by limiting further the situations in which the government rather than industry might initiate a complaint proceeding.

5.10 The Panel noted that governments likewise employed objective criteria when defining the exception for "regional industries" in Article 6:7 of the Code. Instead of providing flexible authority to make an exception whenever economic analysis could demonstrate a separation of markets, the exception in Article 6:7 limits the exception to situations which can satisfy two quite specific criteria: (a) the regional producers must sell substantially all their production in the region, and (b) substantially all the needs of the region must be supplied by the regional producers.

5.11 Most important, the Panel found a similar preference for objective criteria in the negotiating history of the "domestic industry" concept in Article 6:5. Once again, the relevant negotiating history was that of the 1967 Anti-Dumping Code, from which the key terms of Article 6:5 were taken verbatim. In support of its view that governments intended the Code to be interpreted in a flexible manner, the delegation of Canada pointed to several statements in which governments called for a flexible definition of "domestic industry", a number of which objected to a definition based on the "like product" concept as too narrow.<sup>2</sup> Notwithstanding this frequently stated position, however, the text finally agreed to by governments contained the narrow definition of "domestic industry" based on the "like product" concept, as well as the instruction, now contained in Article 6:6, that injury must be appraised in terms of the narrowest product group for which production data is available.<sup>3</sup> Moreover, this narrow definition was made mandatory. The text (which is now Article 6:5 of the Code) stated that "the term domestic industry shall be interpreted as referring to the domestic producers as a whole of the like products".<sup>4</sup> The word "normally", which was used elsewhere in the 1967 Anti-Dumping Code to indicate some flexibility of application,<sup>5</sup> was once considered for the definition of "domestic industry" as well<sup>6</sup> but was omitted from the final text. Viewing this negotiating history, it would be difficult to conclude that governments did not appreciate the rigorous character of the legal standard they were adopting, or that they intended it to be interpreted flexibly.

5.12 In the Panel's judgement, the interpretation proposed by Canada would introduce an element of open-endedness into the Code's definition of "domestic industry" of just the kind the code drafters had

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<sup>1</sup>TN.64/NTB/W/10, p.3 (19 April 1966).

<sup>2</sup>e.g. TN.64/NTB/W/12/Add.3, p.4 (Canadian objection to "like product" test and proposal to define domestic industry as "producers of competitive products"); id. Add.5, p.11, (United States objection to "like product" test and proposal to extend relief to any producers "if their product is in sufficiently close competition with the imports to cause them to suffer material injury.").

<sup>3</sup>Anti-Dumping Code of 1967, Articles 4(a) and 3(d) respectively.

<sup>4</sup>Id. Article 4(a), emphasis added.

<sup>5</sup>e.g. Article 2(f).

<sup>6</sup>"Draft International Code on Anti-Dumping Procedure and Practice: Note by the United Kingdom", Spec(65)86 (7 October 1965), p.13, Provision 12(a-c).

been concerned to avoid. The principle underlying the Canadian interpretation was that relief ought to be made available to input suppliers when they suffered injuries from subsidized imports equivalent to the injuries normally suffered by those who produce end-products. Canada was asserting that this principle applied only to the situation described in paragraph 5.5 above. The Panel was not persuaded, however, that this situation was so unique that it could be distinguished from many other claims for relief that could be advanced under the same principle. There was no reason to believe that the degree of injury suffered by input suppliers meeting the Canadian criteria would be any greater than the degree of injury subsidized imports might cause to input suppliers in any number of other cases.<sup>1</sup> Nor was any greater-than-normal degree of injury required to satisfy these criteria. In the present case, for example, the criteria had been satisfied by a "threat of injury" finding involving a product which was only one of several products produced by the same production facilities<sup>2</sup>, accounting for between ten and twenty-five per cent of the overall revenues earned by those facilities. Nor, finally, was there any basis for limiting this exception to cases involving processed agricultural products. Although all the cases called to the Panel's attention had involved processed agricultural products, there was nothing in the text or in the negotiating history of the Code that could justify a special rule for such products. The Panel did not, of course, question Canada's declared intention to limit the exception to cases meeting the three criteria indicated. The Panel's decision, however, could only rest on principles of general applicability. In the Panel's judgement, any principle justifying the Canadian exception would open the door to claims of standing by a substantial number of other input suppliers.

5.13 In sum, the Panel concluded that both the text and the negotiating history of the relevant Code provisions made it impossible to accept Canada's contention that governments intended the concept of "domestic industry" to be interpreted with sufficient flexibility to permit treating input suppliers as "producers" of the like product when economic circumstances warranted. The Panel therefore found that Canada's interpretation of the term "producer" in this case was inconsistent with the relevant Code provisions. The only way such an interpretation could be adopted would be to amend the Code through negotiation.

5.14 The Panel did not agree that adherence to the narrow definition of "domestic industry" in Article 6:5 and 6:6 would cause outcomes to vary according to the degree of vertical integration which happened to exist at a particular time or in a particular country. The definition of "domestic industry" involves two criteria, neither of which depends on vertical integration as such. First, there must be a determination of which product or range of products constitutes the "like product". If the production process for that "like product" happens to be subdivided into two or more separate stages, that fact will not mean that each stage must be considered a separate "domestic industry" as long as the products at the various stages are enough "like" each other to be considered different forms of the same "like product", the separate production stages will all be part of the same "domestic industry". The second criterion - whether the production process for the "like product" can be separately identified - is likewise independent of vertical integration. If the process of production for one "like product" can be separately identified, it will be treated as a separate industry whether or not it is owned in common with parallel, earlier or subsequent production lines. The only case in which the fact of common ownership will affect the definition of industry will be the case in which common ownership results in such a complete

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<sup>1</sup>The criterion requiring that the input in question account for "a substantial portion of the value of the end-product" has nothing to do with the severity of the economic harm that subsidized imports may cause to any particular input supplier. In addition, while the fact that an input has "no economically viable alternative uses" is certainly relevant, the existence of an alternative market will cushion the impact of subsidized imports only to the extent that prices in the alternative market are equal to or higher than the import-depressed price in the principal market.

<sup>2</sup>The manufacturing beef inputs sold by cattlemen (culled cows and bulls from the cow-calf and dairy sectors and the trimmings from the feedlot sector) were not the product of separately identifiable production facilities. They were essentially by-products of the cattlemen's primary operations.

integration of production processes that it is impossible to analyze each one separately.

5.15 The Panel did not consider that the definition of "domestic industry" outlined in the previous paragraph was in conflict with the Panel Report in "New Zealand - Imports of Electrical Transformers from Finland".<sup>1</sup> The statements in that report which appear to be at odds with this definition were not written with direct reference to Articles 6:5 and 6:6.<sup>2</sup> The actual conclusion in the case - that all product lines of the transformer manufacturer had to be considered when assessing material injury - was not in itself inconsistent with the definition of "domestic industry" adopted in this report, because whenever there are parallel product lines within a single firm, there will always be an issue as to the true separability of those production lines depending on the interchangeability of production resources.

5.16 Finally, the Panel did not agree with the argument that the definition of "domestic industry" in Article 6:5 should be interpreted to be congruent with the definition of "primary product" in Ad Article XVI(B)2 of the General Agreement.<sup>3</sup> Essentially the same argument had been considered by an earlier panel, in "United States - Definition of Industry Concerning Wine and Grape Products".<sup>4</sup> Recognizing that the Committee has so far neither approved nor disapproved the conclusions of that earlier report, the Panel was nonetheless in agreement with the conclusion stated in paragraph 4.5 of that report, notably the view that the two provisions had entirely separate origins and served separate purposes.

5.17 On the basis of the findings reached above, the Panel concluded:

- (i) the term "producer" in Article 6:5 of the Code could not be interpreted to include the cattle producers represented by CCA as "producers" of manufacturing beef;
- (ii) the cattle producers represented by CCA could not therefore be considered as part of the "domestic industry" for the purpose of the Article 2:1 requirements defining standing to complain and the Article 6 requirements governing the determination of material injury; and
- (iii) accordingly, the imposition of countervailing duties based on a petition of the CCA, and also based on a determination of threat of injury to the cattle producers represented by the CCA, was not in conformity with Canada's obligations under the Code.

The Panel suggests, therefore, that the Committee recommend that Canada terminate the outstanding countervailing duty order on manufacturing beef from the EEC, and that it refund any duties collected under that order.

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<sup>1</sup>BISD 32S/57.

<sup>2</sup>The dispute was governed only by Article VI of the General Agreement, because one of the parties was not a Party to the Anti-Dumping Code of 1979.

<sup>3</sup>See paragraph 4.1 above.

<sup>4</sup>SCM/71 (24 March 1986).