ANNEX F

EXECUTIVE SUMMARIES OF THE ORAL STATEMENTS
OF THE PARTIES - SECOND MEETING

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ANNEX F-1

ORAL STATEMENT OF THE EUROPEAN COMMUNITIES

(25 June 2004)

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1. Korea makes increasingly reference to the “financial and economic turmoil” the “assistance of the IMF in resolving the financial crisis or the fact that other Members also subsidised their shipyards as an excuse for granting subsidies to its shipyards. Why does Korea invoke these circumstances although the SCM Agreement does not provide for justification on these issues?

I. PROHIBITED SUBSIDIES

A. MANDATORY/DISCRETIONARY ISSUES

2. Contrary to the suggestions of Korea, the European Communities attaches great importance to its claims against the KEXIM legal framework and its subsidy programmes “as such”.

3. The European Communities does not accept that measures can be brought outside the scope of the WTO Agreement (or dispute settlement) simply by introducing an element of discretion.

4. Whether a measure is inconsistent with a WTO obligation must depend on the characteristics of the measure and the terms of the WTO obligation in question. A discretionary measure must surely be inconsistent with a provision that prohibits such discretion. For example, a discretion to impose antidumping duties at a level of treble the dumping margin is inconsistent with the obligation in Article 9.3 of the Antidumping Agreement that “the amount of the anti-dumping duty shall not exceed the margin of dumping” especially when interpreted in the light of the obligation in Article 18.1 that “no specific action against dumping of exports from another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement.” On the other hand, a power for a government body to grant subsidies, without more, does not violate the SCM Agreement because there is no prohibition on granting subsidies.

5. The so-called mandatory/discretionary doctrine cannot overrule the conclusion reached from an interpretation of the text in accordance with the principles of the Vienna Convention. The Appellate Body has already warned against the mechanistic application of this doctrine and expressly left open the possibility that “discretionary” measures may violate WTO obligations. It has also held that an assessment of the compatibility of a measure cannot end with the conclusion that it is discretionary but must continue with an examination of the effects of the measure.

6. It is true that there exists a presumption of good faith in international law and the so-called mandatory/discretionary doctrine may be a manifestation of it. However, there is by no means a presumption of bad faith when it is assumed that a government or public body will act in accordance with the directions addressed to it in its governing law. It does not matter that it has some discretion not to do so always or systematically, since this discretion must be exercised in accordance with the law.

7. If one wants to try to establish a principle about what measures are subject to dispute settlement and which not, the relevant characteristic is, in the view of the European Communities, whether the measure is normative in relation to the behaviour covered by the WTO obligation in question. That is, does the measure set out the principles that govern or influence how the WTO Member will act in some situation? If the action of the WTO Member is determined according to principles that are inconsistent with those that it has agreed to follow in concluding the WTO Agreement, so that the action will at least in some cases be inconsistent with that agreement, then that measures will be inconsistent “as such” with the WTO Agreement.

8. The consistency of a programme with Article 3 of the SCM Agreement depends on the rules governing the programme and indeed the purpose that it is designed to achieve. It is not necessary that the programme should lead to an export subsidy in every single case (or even a “representative” number of cases), although the fact that there are some such cases is an important confirmatory element.
9. Whether or not every APRG and every pre-shipment loan will be an export subsidy is not determinative (although the European Communities has demonstrated many such cases). What is determinative is that the rules according to which the scheme operates may provide exporters with a benefit – indeed they are designed to do so. These schemes are only open to exporters and provide important advantages that are not available on the same terms on the market. They both provide exporters with important financing facilities for export contracts in the critical period before (properly so-called) export credits and export credit guarantees become available. Even if exporters do not always use these facilities (when alternative finance is more conveniently available), the availability of these programmes provides assurance that if market conditions were to change, finance from KEXIM would still be available at the pre-established conditions. In this respect, it is important to note that Article 3.2 of the SCM Agreement prohibits the maintenance of export subsidy programmes, even where they do not result in grants of export subsidies.

10. Turning now to the other “as such” claim – that against the legal framework of KEXIM – let me first say that the European Communities recognises the far-reaching nature of its claim but considers that it is justified in the circumstances. KEXIM is in reality a funding mechanism for directing state resources into the promotion of exports on better terms than commercial banks would offer. It is directed to do so on the basis of its interest rate guidelines rather than at market rates and at below cost rates when “inevitable for maintaining the international competitiveness to facilitate export”.

B. BENEFIT

1. KEXIM as such

11. KEXIM as such is a benefit because exporters are provided with a bank that enjoys huge amounts of government money and unlimited state guarantee with a mandate to promote exports and the requirement to disregard market principles where necessary to support the export competitiveness of key Korean industries. The existence of such a body the work of which is not explicitly limited to either market principles or to OECD standards is a very significant advantage for exporters, in particular shipbuilding which is in Korea an export oriented industry.

2. APRG and PSL Programmes as such

12. The possibility of obtaining a preshipment loan involves a tremendous advantage for shipyards because they can then offer tail-heavy payment terms with the majority of the payment delayed until delivery. Contrary to what Korea and Drewry want to make the Panel believe, tail-end schemes have become common in recent years on the shipbuilding market. Tail-heavy payment implies that the payments to the shipyard are not sufficient to fund the cash flow during production and financing will therefore be required. Pre-shipment loans (in the form of credit-lines) enable Korean shipyards to accept tail-heavy payment terms. The provision of this “financial product” provided by KEXIM that is not offered by other commercial banks confers a very significant benefit. The existence of the APRG and pre-shipment loan programmes provide financial and thereby economic stability to shipyards.

3. Individual Grants

13. The European Communities noted that it had adequately rebutted Korea’s argument in the second written submission, but wishes to draw the Panel’s attention to a pattern that runs through them: Korea’s non-cooperation in providing the necessary information to adjust the market benchmark in terms of duration and collateral. The European Communities asked about collaterals as early as the Annex V procedure. Korea did not respond. The Panel gave Korea a further opportunity to submit “internal documentation” concerning KEXIM’s review/authorisation of a few transactions,
including worksheets and other documentation showing calculations of the interest rate and other terms, including consideration of collateral”. Korea contented itself with providing the minutes of the Board of Director’s meeting and noting that “it is not KEXIM’s policy to keep and maintain worksheets and similar documents.”

Another tactic of Korea to obstruct the European Communities’ *prima facie* case on benefit regarding individual transactions is the frequent “clarification” of facts once it realised that it had mistakenly failed to withhold information that could be valuable to the European Communities’ case. The European Communities considers that it has done more than making a *prima facie* case and fully rebutting Korea’s defence on the issue of benefit by taking full account of any differences in duration and collateral. Korea has not rebutted the EC *prima facie* case in a substantiated manner, e.g., by selecting some transactions and by providing independent expertise and supporting documents, e.g., on the value of the collateral - but as Korea admits, KEXIM does not keep such materials.

C. SAFE HAVEN

14. Korea does not respond to the EC argument that APRGs and preshipment loans are not export credit instruments envisaged by items (j) and (k).

15. In making APRGs and preshipment loans, KEXIM assumes a risk that relates to the creditworthiness of the domestic exporters. Export credit financing referred in items (j) and (k) however is different in a fundamental respect – it concerns foreign risk. The underlying rationale of these provisions is that domestic banks typically do not have the means of assessing overseas risks of a potential buyer of an export product (or of recovering money abroad). In order to ensure the functioning of a free world market it is essential that overseas buyers have access to financing.

16. The approach taken by the OECD (and WTO) was to harmonise the specific instruments for export financing (guarantees and credits) and to allow the activities of state agencies in this few particular market segment. Korea itself acknowledged that export financing within the meaning of the OECD Arrangement forms only a minor part KEXIM’s financial services provided to promote exports.

17. Items (j) and (k) of Annex I to the *SCM Agreement* cannot justify the provision of export subsidies to the producer through additional financing instruments that cover the domestic risk of the producer as provided by KEXIM.

II. ACTIONABLE SUBSIDIES

18. The European Communities has presented *prima facie* evidence demonstrating that Korea has provided actionable subsidies to its shipbuilding industry, and has rebutted Korea’s contentions to the contrary. In particular, the European Communities has demonstrated that public bodies and entrusted or directed private bodies have made financial contributions to three Korean shipyards that provide a benefit, and that these subsidies were specific within the meaning of the *SCM Agreement* and caused serious prejudice to the European Communities’ interests.

A. FINANCIAL CONTRIBUTION

19. The European Communities has demonstrated that that KEXIM, KAMCO, KDB, IBK, KDIC, and BOK were public bodies that acted pursuant to government policy when participating in the corporate restructurings. We have explained that these bodies are subject to government control beyond ownership, pursue public policy objectives set by the Korean Government, and are entitled to unlimited governmental guarantees of losses. We have also shown that entrusted or directed private bodies involved in the restructuring provided financial contributions to the three Korean shipyards.
20. The European Communities has provided evidence that the financial institutions involved in restructuring of the shipyards were unable to act independently, including the following:

- letters from the Korean Government to the IMF indicating that public funds would be withheld from banks that did not participate in corporate restructuring;
- acknowledgement by a Korean bank that the Government’s influence would cause it to make loans that it otherwise would not;
- a signed commitment by banks to participate in restructurings;
- Government decrees requiring bank participation in financial stabilisation;
- an explicit Government policy of supporting failing companies through debt for equity swaps; and
- statutory limits on the discretion of banks to make decisions relevant to the restructuring.

21. The EC has demonstrated that the Korean Government leveraged its multiple roles as decision-maker, legislator, executive, regulator, shareholder, capital injector, guarantor, and lender to ensure that credit was provided and debt was forgiven for the failing shipyards.

B. BENEFIT

22. The European Communities has presented reasonable market benchmarks to measure the benefit of these financial contributions to the Korean shipyards. This benchmark is based on the conduct of investors outside the reach of the Korean Government’s tremendous influence. It showed that the Korean shipyards received a benefit because they paid less to be relieved of their debts to domestic creditors than they would have under fair market terms.

23. With respect to Daewoo, the European Communities logically compared the value of the debt with the value of the equity, which was based on the opening price of the Daewoo-SME stock on the first day of trading. This comparison, which is the closest market benchmark available, shows that creditors swapped debt for equity and did not receive market return. The European Communities has also provided additional evidence to reinforce the benchmark based on an Australian company’s offer to purchase the company.

24. Daewoo’s creditors (public bodies and entrusted or directed private bodies) conferred a benefit on Daewoo by paying too much for their equity. The change of ownership, therefore, was the subsidy. The creditors of Samho-HI/Halla-HI, on the other hand, once they became equity holders in the shipyard, conferred a benefit by accepting too little for their equity when they sold to Hyundai-HI. In addition to conferring a benefit, this transaction did not extinguish the benefits from the subsidies.

25. Korea erroneously asserts that the European Communities failed to account for debt repayments by the shipyards when calculating the net value of the benefit. With respect to Samho-HI/Halla-HI, for example, there was no debt repayment until the corporate reorganisation concluded in September 2000. As for Daewoo, the plan provided a grace period until the end of 2002. Indeed, because the benefit is composed primarily of the debt-for-equity swap and the negative net asset value of the remaining company, there was no reason to take into account the amount of debt repaid.

26. Korea erroneously argues that the actions of KAMCO, in purchasing non-performing loans of foreign creditors at higher prices than those of domestic creditors, are irrelevant to the benefit analysis. This disparate treatment shows that domestic creditors demanded less for loans than the
foreign banks because domestic banks were influenced by the Government. Moreover, the purchase and anticipated purchase of these loans from Daewoo’s creditors, for example, cleansed the creditors’ balance sheets in a manner that would not have been possible absent KAMCO’s actions.

27. In addition, Korea has failed to rebut the EC’s evidence that Daewoo benefited from a specifically targeted tax exemption valued at KRW 236 billion.

C. SERIOUS PREJUDICE

28. The European Communities has shown that the subsidies to the Korean shipyards have caused serious prejudice to the European Communities’ interests by causing significant price suppression and price depression in the same markets. In response, Korea submitted a report by its consultant, Drewry Shipping Consultants (“Drewry report”), which attempts to prove that:

- Korean and EC yards do not compete;
- commercial ships are so different from each other that a meaningful economic comparison between products is not possible;
- price suppression and depression do not exist in the relevant product markets;
- past price developments are not related to Korean subsidisation; and
- Korean yards are more competitive than EC (and other) yards.

29. Careful scrutiny of the Drewry report, however, reveals that it:

- provides a large quantity of irrelevant information and data;
- represents the European Communities’ positions in a subjective and biased manner;
- bases the like product analysis entirely on the end use of vessels, despite the fact that this end use frequently changes over the lifetime of a ship, and its like product analysis fails to appreciate the necessity for a supply side perspective;
- uses multiple contradictory analytical methodologies;
- basically denies that an analysis of real shipbuilding costs is possible; and
- contradicts itself and Drewry’s own prior analysis of the shipbuilding market.

1. Same geographical and product market

30. The European Communities has demonstrated that the reference to “the same market” in Article 6.3(c) of the SCM Agreement refers to both the same geographic market (i.e. the world market in the case of shipbuilding), and the same product markets.

31. As for the geographic market, even Korea’s own expert report acknowledges that ships are built “in a world market under open market competition.”

32. With respect to product markets, the European Communities has presented evidence showing that (a) LNGs, (b) container ships, and (c) product/chemical tankers (not including pure chemical tankers) are three discrete product markets. Korea has failed to rebut the relevance of these
categories, but continues to argue that the existence of different sizes of ships necessitates a further subdivision of the product market.

33. As with the product definitions in the context of an anti-dumping or CVD investigation, claimants under Article 6.3(c) of the SCM Agreement must be accorded a certain degree of flexibility. As long as the complainant identifies markets or products that are reasonable and coherent, the Panel should accept that definition. The Panel should reject the complainant’s proposed definition only if it would make a market analysis impossible. Far from impossible, the European Communities’ product market definition is used by a number of market analysts, including Drewry itself.

34. Moreover, unlike lost sales claims, there is no need to demonstrate head-to-head competition in price depression or suppression claims. This is especially true in the shipbuilding industry, where the price is set at the time that a ship is ordered, rather than after a product has already been produced. As long as a company is capable of offering to produce a ship, it does not matter whether it has produced that ship in the past.

35. Korea’s narrow product market definitions contradict reports from the leading experts in the commercial shipbuilding industry. It is obvious that ships, as made-to-order products, will show variations in size and specifications. But shipbuilders can easily accommodate these variations in the course of their normal business. From a technical point of view, all commercial vessels share the same key product characteristics. They have a welded steel hull and superstructure, they are powered by similar types of engines; they have to fulfil the same navigational and regulatory requirements; and they are subject to the same principal construction rules put forward by the classification societies.

36. Although it is not necessary to demonstrate the existence of head-to-head competition, the European Communities has shown, as do Korea’s own tables, that EC and Korean shipyards often do sell ships in the same product markets.

37. Without justification, Korea has requested adverse inferences based on the European Communities’ alleged failure to produce detailed information about the many EC shipyards that produce vessels within the scope of the dispute. The European Communities did in fact provide sufficient evidence to the panel, but, aside from this, the request for adverse inferences is inappropriate, because the claims do not require proof of head-to-head competition, but only that prices have been suppressed or depressed at the stage of bidding.

38. Drewry’s attempt to support Korea’s position that EC yards are concentrating on different vessels is undermined by the realities of the industry and by Korea’s own arguments in this case. Indeed, the orderbooks of Korean yards show that they, like the major EC yards, are universal yards. Drewry’s own tables and statistics thus reveal that Korean and EC shipyards build vessels in the same markets.

39. In addition, Drewry argues that the product market is highly segmented by exaggerating differences on the demand side of the market (i.e. end uses and ship specifications) and ignoring similarities on the supply side (i.e. the capability of modern shipyards to produce a wide variety of vessels). This argument, however, is contradicted elsewhere in the report where it speaks of standardised ship types with regard to container ships and LNG carriers, and ships built on market speculation or "commodity vessels". Ships cannot be commodities on the one hand and too specialised to compare on the other.

2. Price Depression/Suppression and Causation

40. The European Communities has already demonstrated that the Korean subsidies have caused significant price depression and suppression of LNGs, and significant price suppression of container ships and product/chemical tankers. Based on this evidence, the European Communities has shown
that, but for the massive subsidies, the tremendous overcapacity maintained by the Korean shipyards would have been significantly reduced. Such a reduction in capacity, given the large market share of the restructured Korean shipyards, would have had a significant effect on prices in the three product markets at issue.

41. Korea fails to acknowledge the common sense approach to finding adverse effects of subsidies, which is reflected in Articles 6.1 and 6.2 of the SCM Agreement. It is, for example, a basic principle of economics that the maintenance of capacity will lead to lower prices (all other variables being constant), or that direct forgiveness of large debts will affect prices by reducing the producer’s costs. The SCM Agreement does not require the Panel to perform complex calculations that will yield obvious results.

(a) Korean shipyards have influenced world market prices

42. In order to conceal the true market share of the three Korean shipyards in question, Korea and Drewry assess market share according to the number of ships ordered and produced rather than the combination of physical size and work content (expressed in compensated gross tonnes (CGT)) of ships ordered and produced, which is the standard industry method. Because Korean yards tend to produce ships at the upper ends of the relevant size ranges, Korea’s method understates their market share. The European Communities’ use of CGT to measure market share follows the practice of the OECD, as well as the Korean Shipbuilders’ Association and Drewry, themselves.

43. Measured according to size and work content, the three shipyards primarily at issue in this dispute together account for about one-third of the orderbook in Korea and twelve percent of the global orderbook. By way of comparison, the volume of orders in the three Korean shipyards alone is equivalent to ninety percent of the orderbook of all the Chinese shipyards and seventy-five percent of the orderbook of all EC shipyards. With this level of market share, there is little doubt that the three Korean yards exercise considerable influence over world prices.

44. The influence of the three Korean yards on world prices is even greater when viewed in the context of the specific product markets, which have a small number of suppliers. For example, Daewoo-HI/Daewoo-SME alone accounts for 32 per cent of the global orderbook for LNGs. Daewoo-HI/Daewoo-SME, Samho-HI/Halla-HI, and Daedong/STX are three of the five Korean shipyards that collectively control nearly two-thirds of the market for LNGs. Samho-HI/Halla-HI accounts for 7 per cent of the global orderbook for container ships, and, together with its parent, the Hyundai group, accounts for 33 per cent of the orderbook. Daedong/STX and Samho-HI/Halla-HI are two of four Korean shipyards that control 60 per cent of the market for product/chemical tankers. These statistics and other evidence provided by the European Communities demonstrate that the three Korean shipyards have a large enough market share to exercise significant influence over the world price of tankers, containership, and LNGs.

(b) Temporal link

45. Korea’s arguments about the absence of a temporal link between the subsidies and the price effects ignore the fact that pressures on price in the shipbuilding industry are first felt when price offers are presented, and well before a contract is actually secured. This bidding usually takes place several months or even more than a year before the contract is signed. Moreover, there is generally a lag of some years between taking an order and building the ship. Many of the orders taken by Korean shipbuilding in 2003, for example, are for delivery in 2007 or 2008.

(c) Specific effects of the restructuring subsidies on prices

46. Simply stated, the subsidies enabled the shipyards to remain in operation and gave them economic stability in a particularly cyclical and unstable business. Drewry itself stated in a 1999
report that Korean yards were almost solely responsible for increases in capacity and that investments in these yards were viable only as long as the companies did not face the true cost of borrowing (the banks did instead).

47. Korea also confirms through Drewry’s report that shipyards with overcapacity tend to offer low prices, a factor that lies at the base of the European Communities’ assessment of the problems in the world shipbuilding market.

(d) Assessment of shipbuilding prices and costs

48. The European Communities has presented accurate and comprehensive information regarding the various factors that influence shipbuilding prices and costs. Korea, by contrast, fails to take account of overhead costs, or the depreciation and interest charges. The European Communities’ evidence of the rising costs of ship production for the three Korean yards is based on consideration of all relevant costs, and accounts for the cost-advantages enjoyed by those yards. The European Communities and FMI stand by the results of their cost modelling and market and price analyses; all efforts by Korea to disprove these results have failed.

49. With respect to prices, Drewry fails to refute directly the price indices offered by the European Communities for each of the three product markets. Instead, Drewry argues that it is impossible to derive meaningful price indices for these product markets, even though Drewry uses these very same indices in chapter 8 of its report and in its own non-commissioned works. The European Communities has shown that a convergence of the following three factors should have caused shipbuilding prices to rise (in the case of product/chemical tankers, container ships, and LNGs) or not to fall (in the case of LNGs): increasing volume, increasing producer costs and high customer earnings.

(e) Valuation of subsidies

50. Although the SCM Agreement does not require a complainant to calculate the precise value of subsidies for purposes of demonstrating serious prejudice, the European Communities nonetheless has done so. Korea disputes the calculation of the benefit from the restructuring subsidies to Daewoo, arguing that it improperly looks beyond the liabilities of the core business of shipbuilding. The European Communities’ point, however, is that the restructuring would not have occurred if the creditors had acted pursuant to market considerations, and the company would have retained all of its liabilities, whether or not related to its “core” operations.

51. With respect to the calculation of benefit to Samho-HI/Halla-HI, Korea disputes the European Communities’ stock valuations. In fact, this valuation must be considered correct unless Korea admits that Rothschild made an incorrect valuation of Samho. The European Communities has already explained why Korea’s proposed valuation based on net asset value is inadequate and further notes that no consultant has ever used this methodology to value shipyards.

52. Korea’s reference to the long-term benefit of investments in facilities is a red herring, because Korean shipbuilders made no such investments after 1996. Based on investments in tools, machinery, and equipment for ships, it is reasonable to assume that the subsidies granted after 1997 had a useful life of about 10 years.

53. Korea fails to rebut the European Communities’ argument that KEXIM pre-shipment loans and APRGs contribute to over-capacity, and therefore price suppression and depression. Korea states that KEXIM pre-shipment loans were granted for only “a limited number of shipbuilding projects” even though it supplied a list of hundreds of pre-shipment loan transactions in the Annex V process.
54. With respect to Korea’s attack of the European Communities’ attempt to quantify the value of a KEXIM pre-shipment loans and APRGs, the European Communities has already explained that it made reasonable estimates based on the limited evidence provided by Korea. Even on the basis of the new information on disbursement dates the quantified value remains high.
ANNEX F-2

ORAL STATEMENT OF KOREA

(28 June 2004)

I. INTRODUCTION AND EVIDENTIARY MATTERS

1. Korea is presented at this Second Meeting with a difficult task brought on by the litigation tactics of the EC claiming that it was not required to demonstrate the necessary facts to establish a prima facie case. The EC claims that a prima facie case can be based on simple assertions of facts that do not need to be proven if undisputed by the respondent. Hence, all a complainant would have to do is to make allegations which would shift the burden to the respondent to rebut them. Only then would the complainant need to adduce any evidence to support its claims. The EC further argued at the First Meeting that it need not demonstrate elements of its case that it considered “obvious”, but then refused to identify just which elements those were.

2. The EC’s position could not be more contrary to the jurisprudence of the WTO. This is summarized by the Appellate Body statement in US – Wool Shirts and Blouses to the effect that “[W]e find it difficult, indeed, to see how any system of judicial settlement could work if it incorporated the proposition that the mere assertion of a claim might amount to proof.”

3. Following from its legal proposition regarding the burden of proof, the EC provided a virtually fact-free First Submission and oral presentation at the First Meeting. This forced Korea, arguing in the alternative and in response to Panel questions, to provide a considerable amount of argumentation and facts. Only then, did the EC submit a large number of new arguments and supporting “facts” in its Second Submission. This left Korea with the task of presenting rebuttal data at the Second Meeting in response to EC material that should have been provided at earlier stages of the dispute to support establishment of the EC’s prima facie case in accordance with WTO rules and jurisprudence. Korea has responded as thoroughly as possible with arguments in the alternative, while reserving all of its rights regarding the burden of proof, due process and the Panel’s Working Procedures. Korea specifically recalls the Appellate Body findings in Japan – Agricultural Products II and Chile – Price Bands to the effect that the Panel is not to use its investigatory powers to make the complainant’s case for it nor to answer affirmatively claims that have not been effectively advanced by the complainant. Particularly in light of the difficulty of benchmarking during the period of the financial crisis, Korea also recalled the reasoning of the panel in the US – Section 301 dispute to the effect that, if faced with a situation where the arguments of two parties left it in uncertainty or equipoise then, logically, the proper allocation of the burden of proof would mean that the benefit of the doubt would go to the respondent.

4. It is useful to step back and look at what is really going on in the shipbuilding markets -- recognizing, of course, that it plays out somewhat differently for each product. If there is indeed a problem with subsidies, it is with the EC that has splurged hundreds of millions of euros of subsidies of all forms. The EC Commission acknowledges in its periodic shipbuilding reports that EC subsidies have actually caused significant overall harm to the EC industries. In contrast, Korea has built a vibrant set of shipbuilding industries that compete fiercely but fairly based on efficient, flexible labour and a vastly lower cost structure. All of the trend lines the EC refers to concerning the competitiveness of the Korean industries are in existence from the late 1980’s and early 1990’s. There is nothing new and different about the period 1997-2001 except that the whole Korean economy went through a terrible financial crisis that spread out of Southeast Asia and nearly brought
the whole country to its knees. In this financial crisis, the EC has seen an opportunity to extract a competitive advantage that it could not through competition in the marketplace.

5. Regarding the issue of “public bodies”, Korea agrees with the EC that the question of government ownership can be a good starting point. However, the EC has developed a non-treaty based test that is little more than variations on the theme of government ownership. In order to properly define the term, the obvious place to start is the treaty text itself. It sets up three categories of entities. At one end of the spectrum are the organs of government themselves. This would be something such as the Finance Ministry, for example. At the other end would be unarguably private entities. In between these poles exists something else referred to as a “public body” and the question becomes how to evaluate this term. The first point is that public bodies and the government are grouped together. Indeed, they are collectively referred to as “the government” in Articles after Article 1.1. As Korea has noted, the obvious implication of this is that it refers to actions that are essentially “governmental” in nature. Moreover, it also clearly implies that there are some actions that such entities can take which are not governmental action. That does not leave any gaps in the overall treaty scheme, despite what the EC alleges, for even if an entity is not considered a public body for purposes of the measure at issue, there is still the possibility of demonstrating that the government entrusted or directed the actions in question. Thus, while there is no gap in coverage, there is a distinction in the manner of proof. And this is where the EC ran into trouble for it has no evidence at all of entrustment or direction by the government.

6. For purposes of providing interpretative guidance, Korea refers the panel to Articles 4, 5 and 8 of the International Law Commission’s Articles on State Responsibility that were commended in a December 2001 Resolution by the UN General Assembly to the membership for consideration. These three Articles provide a close parallel to the language of Article 1.1 of the SCM Agreement. In particular, Article 5 refers to entities empowered by a State’s laws to exercise governmental authority; it further notes that a measure at issue will be considered state action only to the extent it was taken pursuant to such authority. The Commentaries to the Articles note that this was meant to cover para-statal entities that act in place of the organs of state. Thus, the Articles outline a two stage test that corresponds closely with the logic of the treaty language. Korea also noted again that this approach was consistent with the definitions provided in the GATS Annex on Financial Services. Korea also pointed out that the EC had presented its arguments against KEXIM and then applied them mutatis mutandis to the other government-owned banks, thereby improperly lumping everything together; this clearly did not satisfy the EC’s burden of proof.

7. Regarding “private bodies” acting on entrustment or direction of the government, Korea noted that the EC continued to make a straw man argument regarding the admissibility of circumstantial evidence. Korea agrees that circumstantial evidence is admissible, but specifically noted that the legal probity of such evidence was suspect the further it got away from direct evidence. The real issue was whether the evidence of whatever type demonstrated conclusively that there was explicit and affirmative entrustment or direction by the government to the private entity in question to take the measure at issue. This is the logic of the findings by the panel in US – Export Restraints. Korea noted that the EC expressly rejected this idea and proposed a test based on what it referred to as “general direction.” Korea further noted that even under this test, the EC’s “evidence” was mere inference and stereotyping.

8. With respect to the issue of timing of alleged subsidization, Korea noted that the EC was once again setting up a straw man to knock down rather than addressing the real issues at hand. Korea was not arguing that older data was not admissible or that there was some sort of legal bar to discussing it. Rather, the issue was one of evaluating the evidence. In this regard, it was clear that the period of the financial crisis was sui generis. Korea’s concern is that the EC was attempting to take advantage of the financial turmoil during this period to extract a competitive advantage that it could not in the marketplace. Specifically, the EC was comparing factors from outside that period with factors from that period. This was illogical and impermissible. Moreover, the EC was attempting to take
advantage of the difficulty of establishing benchmarks during such a period to argue that any governmental activity during the period was a subsidy. Korea recalled that the burden was on the EC as complainant to establish and demonstrate appropriate market benchmarks.

II. ALLEGATIONS OF PROHIBITED SUBSIDIZATION

9. The EC’s arguments that the KEXIM Act and the two programmes are per se illegal would overturn decades of GATT and WTO jurisprudence regarding the distinction between mandatory and discretionary measures. There is no indication that the Appellate Body intended such a conclusion in the US – Sunset Review dispute cited by the EC. Korea again went through the various provisions of the KEXIM Act and described how they did not result in a mandatory requirement of export subsidization by KEXIM. Korea also reviewed the empirical evidence demonstrating how KEXIM always covered its operating costs (which is, in any event, an issue of cost to government and is not relevant at this juncture) and that KEXIM was in competition with other lenders throughout the period of the inquiry. Korea also reviewed KEXIM’s methods for setting its rates and demonstrated how they could not be interpreted as requiring subsidies; indeed, they resulted in market-based rates.

10. With respect to the APRG programme, Korea noted that there was a general lack of APRG activity during the period of the financial crisis, and that, as detailed in Response 47 to the Panel Questions, while the APRG rates in Korea prior to the Asian financial crisis ranged from 0.1 per cent to 0.2 per cent, KEXIM doubled or more its overall rate to around 0.4 per cent during the crisis, which is composed of the base rate and the spreads. This increase in rates shows that KEXIM adjusted appropriately to reflect the changed circumstances. In contrast, the EC has cited a couple of isolated instances of APRGs from foreign banks that were not representative. There are two ways that APRGs are procured. The first is selection by the shipyard. In such cases, shipyards select the issuer considering, inter alia, the competitiveness of the premium rates proffered and the past transaction experiences with the issuer. In some other isolated cases, the buyer designates the provider of APRGs. Buyers designated a couple of foreign banks right after the onset of the 1997 financial crisis but this practice rapidly subsided as the Korean financial industry regained creditworthiness. These buyer-designated providers generally were not as familiar with the practice and charged higher rates reflecting their ignorance of the companies and the markets. They also followed the standard lending practice of charging country risk premiums which were relatively high during the financial crisis. There also was generally lesser collateral both quantitatively and qualitatively for the foreign banks. The EC admitted that it did not have adequate evidence to support its claims and asked for adverse inferences under the authority of Annex V which is exclusively limited to the issue of serious prejudice. Indeed, this request demonstrated again the abusive nature of the EC’s demands during the Annex V process, a matter Korea still requested the Panel to address. In the meantime, the EC’s request provided an admission against interest regarding the lack of a prima facie case.

11. Regarding the pre-shipment loan programme, Korea noted that the EC had introduced a large amount of new “evidence” regarding its proposed benchmarks. This evidence was not in rebuttal, but was part of the EC’s initial prima facie case. Therefore, the requirements of due process, WTO precedent and the Panel’s working procedures required that it be dismissed. Nonetheless, arguing in the alternative, Korea rebutted the EC’s evidence which was based on bond indices. Korea noted that the bond indices were distinct in a number of ways.

- Despite the fact that the KSDA data for 6 month corporate bond yield rates are available, the EC has intentionally taken 1 year corporate bond yield rates and made distorted adjustments to make them allegedly comparable to the 6 month corporate bond yield rates;

- The EC misapplied the value of Yangdo Dambo collateral;

- The EC misapplied the credit rating for DHI/DSME;
• The EC failed to adjust Samho Heavy Industries’ pre-shipment loan rates for the 100 per cent physical collateral provided; and

• The EC failed to consider the fair value of the other relevant factors that have substantial security value and mitigate the risk for KEXIM’s pre-shipment loans.

12. Korea noted, moreover, that as the financial crisis ebbed, the instruments the EC offered and the pre-shipment loan rates converged as the underlying economic issues meant that they were more closely comparable.

13. Regarding the issue of safe havens, in Korea’s view it was quite clear from the Appellate Body’s statements in Brazil – Aircraft (Recourse to Article 21.5) that such safe havens existed. Unlike the EC, Korea does not consider it appropriate to disregard the Appellate Body’s clear language. The EC has rejected the Appellate Body’s argument with respect to item (k) first paragraph on the basis that Annex I is an Illustrative List and therefore a non-exhaustive list cannot provide a safe harbour. However, the EC then seems to forget this and argues that item (j) does provide a safe harbour. Purportedly, this is because item (j) contains a “proviso”, but that distinction remained unexplained. The EC also contended that item (k) was exclusively in reference to the OECD. Aside from the fact that the OECD is not mentioned, its relevance was limited to the exception of the second paragraph of item (k) and could not be read as defining the broader rule of the first paragraph. In Korea’s view, there is either an a contrario reading of footnote 5 that leads to safe havens in both item (j) and item (k), first paragraph, or there is not an a contrario reading. There is no logical or treaty-based, linguistic way of splitting the interpretation between the two.

14. Korea also noted that there was no basis in logic for distinguishing between the legality based on who receives the benefit. While the EC has claimed that this was a settled matter in the OECD, that was not the case. Other OECD members had raised concerns about not being so formalistic as to create loopholes. Moreover, Korea noted that the EC was explicitly separating item (j) from the OECD. Furthermore, as noted above, there was no legitimate basis for reading OECD requirements into the first paragraph of item (k). Korea had presented ample evidence to demonstrate, as an argument in the alternative, that the APRG and pre-shipment loan programmes satisfied the requirements of item (j) and (k) in such manner as to qualify for the safe havens.

III. ALLEGATIONS OF ACTIONABLE SUBSIDIES

A. GENERAL MATTERS AND RESTRUCTURINGS

15. One of the issues of continued disagreement between Korea and the EC is whether or not a panel can make simultaneous findings that one set of measures are both prohibited and actionable subsidies. In Korea’s view, the unique nature of actionable subsidies claims where actual adverse effects must be demonstrated requires a negative answer because otherwise there will be double-counting of subsidies. Korea notes that the EC asks the Panel to ignore Article 7 as the issue of remedies is not before the Panel. However, Article 7 is part of the context of Articles 5 and 6 and indicates the unique nature of Part III of the SCM Agreement. Article 7.8 states that the remedy can be either removal of the adverse effects or withdrawal of the subsidy. This possibility of removal of the adverse effects is unique in the sense that everywhere else the requirement is bringing the measure into conformity with WTO obligations.

16. In light of this, it is important to look at what happens when there is determination of prohibited subsidization. In such situations, if an export subsidy is found to exist under the terms of Part II of the SCM Agreement, then the only remedy, according to Article 4.7, is withdrawal without delay. Therefore, such subsidy would already be required to be removed by operation of law. If a
panel were, nonetheless, to consider the effects of such a subsidy under Part III, it raises the possibility of an affirmative finding with respect to the other subsidies which might not be, on their own, causing adverse effects. In effect, the remedy under Article 7.8 would already exist. So, this becomes an empty exercise and one that is contrary to the very nature of Part III where there is not to be an affirmative finding unless the subsidies at issue are causing adverse effects.

17. Regarding the restructurings themselves, Korea demonstrated the following:

- The EC has failed to show that the banks are public bodies for purposes of the subsidy analysis
- The EC has created a new standard for direction and entrustment and – by any standard – has failed to show how the Government of Korea directed or entrusted the banks to subsidize the shipyards.
- The EC has failed to show how a financial contribution was provided to the shipyards when debt was switched for equity.
- The EC has failed to show how a benefit is provided to a company through a bankruptcy or corporate restructuring proceeding.
- If there was a benefit, the EC has failed to show how this benefit carried through to the new owners of the companies.
- Finally, the EC has failed to show how the bankruptcy or corporate reorganization proceedings were specific to the three yards.

18. Regarding the issue of benefit in light of changes of ownership, Korea notes that there was nothing in the theory of changes in ownership that the Appellate Body and panels relied upon that limited the decisions in the previous cases to privatizations. Indeed, the Appellate Body was quite clear that privatization was only one example of the theory and, in fact, the one instance where change of ownership was least likely to result in extinguishment of the benefit. In the present case, the net debt was owned by the previous owners who were all wiped out, or virtually so. At that point, the creditors have control of the company. They have effectively written off that net debt and the loans are re-valued accordingly. This is why Korea has spoken about the change in form rather than a change in value. As a result, there can be no financial contribution when the instrument does not represent any change in value. Furthermore, even if this were considered a financial contribution, there is no benefit, because the creditors (i.e., the new owners) received nothing of greater value than what they had before. The EC’s response here is to focus on the alleged benefit to the productive assets themselves, not the persons holding such assets. For example, the EC states that the assets would not have continued in existence but for the alleged subsidy. Of course, this is directly contrary to the findings of the Appellate Body in *US- Lead Bars* and *US -- Countervailing Measures* where the Appellate Body rejected this “but for” argument when it was presented by the United States in those cases.

19. Moreover, the EC in general has offered the Panel its own example of how to do workouts and insolvencies. The EC claims that they must be accompanied by permanent capacity reductions. This does not seem to be the case with the East German shipyards or those of the acceding EC countries. There have been no permanent facility shutdowns in those yards. Furthermore, there is no indication whatever of capacity or production constraints in the recent case of the Alstom bankruptcy. Indeed, all that is evident on the record is the continued generous subsidization of all of the EC shipyards.
20. **Regarding DSME**, the EC has alleged that the Korean government “controlled” the process. However, even if the panel were to agree that mere government ownership of several Korean banks made them public bodies, these entities did not control enough of the outstanding credit to control the process under the prevailing arrangements. The EC also refers to the alleged “control” that the Government of Korea had over all of the banks during the financial crisis. However, despite the EC’s repeated attempts to get the IMF to support the EC’s point, the evidence is conclusive that the restructuring of the financial sector pursuant to the agreement with the IMF was done on market principles and banks restructured their bad loans to maximize value. Thus, any influence of the government had exactly the opposite effect that the EC alleges. The sole piece of “evidence” the EC proposed regarding alleged improper influence was revealed by Korea’s provision of the full quotation by a single Korean bank to be a reference to the real estate sector and even that was specifically noted by the bank’s lawyer not to refer to even the general point the EC was alleging.

21. **Regarding the issue of benefit in the DSME restructuring**, the EC offered a report by its consultant, Price Waterhouse Coopers (PwC) critiquing the workout report done by Anjin, the former Korean affiliate of Arthur Andersen. A response by the authors of the Anjin Report as well as an independent retired senior British banker, Mr. William Lawes, confirmed that the Anjin Report was objective and fair; it was commissioned for the purpose of determining the best commercial, value-maximizing solution to the insolvency of DHI resulting from the credit crunch brought on by the Asian financial crisis. Anjin was required by the terms of its contract to act in an objective manner and there is absolutely no evidence of any sort that it did not do so. Anjin was not directed to come up with any particular answer, but provided an independent opinion as to the relative values of the available options. Mr. Lawes found that the Anjin Report was appropriately done, took into consideration all of the appropriate facts and was overall consistent with just the sort of evaluation that would be expected on the part of banks utilizing the “London Approach” to maximize value in situations of corporate insolvency. Mr. Lawes also confirmed the logical point that the foreign-owned banks were in a fundamentally different circumstance and had every incentive to take a better short term deal but with less long-term potential. Such a decision led to negotiations to sell their debt for as high an immediate payout as possible to those domestic banks, who had more at stake and more time and inclination to follow the workout route which could lead to a greater potential recovery over time. Again, the bargain for a residual amount of warrants demonstrates that the foreign banks recognized this trade-off.

22. The EC continued to argue that the debt-equity somehow “cleansed” the balance sheet of DSME despite the fact that the new owners were the old creditors making it impossible to see what exactly was cleansed. Any further debt could not have resulted in any changes in the debt equity swap as the players and the value were both the same under either scenario offered by the EC. The EC also pointed to the purchase of debt by KAMCO as cleansing the balance sheet. However, it was irrelevant to the balance sheet of DSME for it only resulted in a change of creditors, not a reduction of debt.

23. The EC also challenged the valuation done by Anjin given the allegedly low price offered for the stock of DSME by an objective foreign bidder. The EC referred to newspaper reports of a bid by an Australian company, Newcastle Heavy Industries. Korea rebutted this allegation by showing that NHI actually offered a substantial premium over what the EC alleged.

24. **Regarding specificity**, the EC’s argument was little more than an allegation that the size of the Daewoo group meant that the restructuring was specific. However, the workout approach was broadly available and Korea had earlier submitted evidence demonstrating that a great number of companies availed themselves of the approach. Size alone does not render a procedure specific.

25. **Regarding the alleged tax subsidies in the case of the DHI spin-off**, there was no valuation gain or profit because the DHI assets were simply allocated at “book value” to the two spun-off companies and the remaining DHI. Therefore, because the assets were simply moved from one entity
to another there was no taxable event and no forgoing of any government revenue that was otherwise due. Therefore, Article 45-2 did not confer a benefit. Korea noted that the numbers the EC presented were taken exclusively from a newspaper report and that was not sufficient evidence. Moreover, the number the EC alleged was with respect to all of DHI and did not reflect any allocation between the divisions. Korea further demonstrated that the tax laws in question were not specific to the DSME transaction. If they had been, there would have been no reason to extend them for a further two years after the DHI spin-offs. As noted above, Article 46 of the Corporate Tax Act mandates specific tax treatment with respect to “gain” or “profit” realized to the spun-off company as a result of the “valuation” of assets conducted in the course of spin-off.

26. **Regarding the Samho restructuring**, Korea noted that the EC seemed to drop any reference at all to the role of the judges in the transaction. The reorganization proceeding cannot start unless the court determines that the going concern value of the subject company is greater than its liquidation value. If such is the case, the court has the power to order a receiver to submit a reorganization plan based on the continuation of business activities of the company concerned. If the plan submitted does not conform the provisions of the Corporate Reorganization Act or is unfair, unequal or not feasible, the court may decide not to refer the plan to the meeting of the interested parties for resolution. The court also has the authority to approve or reject the plan adopted by the interested parties. In sum, it is the court that decides whether to permit the subject company to continue its business operations. In order to establish that the court receivership, and any transaction done within the context of the court receivership, was not done at arm’s length or conferred a benefit, the EC needs to show that the judge in this instance did not do his job, that he failed in his legal and fiduciary responsibility to maximize the return on the debt to the creditors. The EC has presented no such evidence. None exists.

27. The EC contradicted its approach to the DSME workout where the EC alleged that the new owners overpaid, by now arguing that the new owners of Samho underpaid. Of course, once again, the real answer is that facts do not support the EC’s allegations regardless of which of their contradictory approaches they choose. In the case of Halla/Samho (as with Daedong/STX discussed later), the court determined that the going concern value was greater than the liquidation value and decided to proceed with the corporate reorganization. This court decision was based on the valuation by Rothschild, a financial advisor, and on Rothschild’s corporate reorganization proposal which was drafted to maximize the debt repayment to the creditors. Moreover, among the many factual errors in the EC allegations was the basic point that the EC neglected to include the assumption of debt in the purchase price of Samho.

28. **Regarding the issue of specificity**, the EC argued that if Article 1.1(a) is satisfied because there was a financial contribution pursuant to government action and that Article 1.1(b) was satisfied in that a benefit has been demonstrated, then Articles 1.2 and 2 regarding specificity are **automatically** satisfied. That is, the EC reads Articles 1.2 and 2 completely out of the SCM Agreement. Obviously, the Panel cannot adopt an interpretation of the treaty that reads whole provisions as nullities.

29. **Regarding STX**, the EC argued that the sale of the company by the bankruptcy court was improper because it was sold to a Korean company. In an unfortunate instance of stereotyping, the EC claimed an “inherent defect” on the part of any Korean company. Korea demonstrated that the sale pursuant to a Recommendation Report by KPMG went to the highest bidder out of five. Of the five, two and perhaps three were non-Korean companies. The EC then reverted back to its unsupportable argument that any result from insolvency other than termination of the company and selling it for scrap was a benefit. Regarding specificity, the EC made the same incorrect arguments that it did with respect to Samho whereby the step of determining specificity was automatically satisfied by a finding of government involvement and benefit.
B. SERIOUS PREJUDICE

30. There is a basic disagreement between Korea and the EC on the issue of whether there is a need for the complainant to demonstrate serious prejudice. According to the EC the treaty contains a very mechanistic test. If any one of the elements of Articles 6.3 (a), (b) or (c) is shown, then the serious prejudice element of the case automatically is satisfied. The complainant need show nothing more. Essentially, the case is over. Of course, this approach requires reading out of the treaty some very important words. The chapeau of Article 6.3 provides that serious prejudice *may* exist when *one or several* of those elements are demonstrated. The EC reads the word “may” to mean “shall”. Indeed, the EC really is replacing it with something more; it is really saying “shall be deemed to exist” because once again the EC is trying to create presumptions as substitutes for proof. It is worth noting that the EC interprets the term “may” in much the same way as it interprets the term “shall” from the now-expired presumption-creating provisions of Article 6.1. Next, the EC reads the “or several” out of the text. If any one element were enough to lead to an automatic and necessary conclusion of serious prejudice, why would there ever be a purpose in demonstrating others? Of course, there would not be. The words “or several” would be totally superfluous.

31. The EC attempts to eliminate the word “serious” from the treaty text. The EC’s only attempt to respond to Korea’s reference to the extensive jurisprudence that confirms that “serious” indeed connotes a higher standard than “material” is to jumble up Articles 5(a) and 6.3(c). Similarly, the EC attempts to read out of the treaty the term “prejudice”. As Korea has noted there is no basis for reading the term prejudice as somehow lower than the term injury. In Korea’s view, the term “interests” refers not only to the state of the complaining party’s industry, but also to something more. The term “interests” is a broader term. Simply put, a complaining Member should not be permitted to potentially adversely affect the terms of sale in third country markets of other Members in this fashion unless it can show that its broader interests are seriously negatively affected.

32. Even more surprisingly, the EC maintains that it does not have to establish like product categories. Korea considers it fundamental to the treaty structure and plain logic that like product categories must be established by the complainant. Unless the complainant does so, there is simply no coherent manner of discussing the elements of the case. The EC argues that Korea’s reference to like product in Article 15.2 of the SCM Agreement and Article 3.2 of the Antidumping Agreement is misplaced because those provisions refer to like products in imported markets. This argument seems to have been pulled from the air, for it is quite illogical and has no basis in the treaty. The EC fails to explain Articles 6.3(a), (b) and (c), as well as 6.4 and 6.5 which all refer to like products and none of which involve importation into the complaining Member’s market.

33. The EC has built its whole case on an argument of price suppression or depression due to capacity issues. However, how can one discuss either capacity or price suppression or depression without rigorously defining markets? Capacity in what products causing price suppression or depression of what products? The EC only provides a bunch of charts of shifting product groups (for instance, at various times the EC has endorsed the Japanese suggestion that there is only one like product category) and even tried to sell the Panel on causation due to a “kink” in a price chart including apparently all commercial ships. Is the reason the EC suddenly decided in the middle of the case to exclude pure chemical tankers from the dispute because of the effect on their pricing charts of inclusion of this product? The EC claims that within the product types that it has distinguished (container ships, product and chemical tankers and LNGs) there is no need to further distinguish by size because vessels of all sizes can be substitutable in many instances on all routes. It thus not only contradicts the size differentiations that are commonly made in shipbuilding and shipping trade but also the statement of its own expert that substitution is rarely possible on a size basis because of the economics of trade and that one seventy thousand dwt ship, for example, is not operationally or economically equivalent to two thirty-five thousand dwt ships. The EC’s reliance on supply substitutability -- claiming that vessels are merely an assembly of steel and that a shipyard can build any type of vessel -- is hardly understandable and is certainly contradictory with the EC’s own
exclusion of all sorts of products from cruise ships to Ro-ro ferries to pure chemical tankers. First, what is a like product must be determined primarily from the demand side based on technical characteristics and their value added for the use of the products as perceived by the user. Second, no single yard in the world claims that it can build all vessels. In reality, EC yards intentionally - well before the corporate restructuring in Korea - concentrated on the smaller like products as well as on high value added niche vessels including cruise ships, ferries or roll-on roll-off vessels. It is equally an arbitrary and broad brush conclusion by the EC to refer to “Korea” in general when the participation of the restructured and non-restructured yards in different like product vessel markets is widely different. This is true all the more in that those like product vessels where there still is some competition between EC and Korean vessels, most, if not all of these Korean vessels were built by non-restructured yards that did not benefit from the alleged corporate restructuring subsidies.

34. Of course, the EC insists on calling it an over-capacity issue. This addition of “over” is nothing but an emotive term that the EC hopes will affect the way the Panel views the market. As the EC has itself acknowledged, there is not an agreed upon way of defining capacity in shipbuilding. In fact, there is general agreement the other way, i.e., that there is no universally applicable or unambiguous way of defining capacity. Any existence of capacity will affect the market whether it is from Estonia or Korea. And, of course, the larger the country’s industry, the larger the impact of production from that country. Obviously, the EC is trying to direct the case away from the issue of the effect of the subsidies and get the Panel to focus on the effect of the products. If it can do that, then under the EC’s approach, the sheer size of the Korean industry today (as should the size of the Japanese industry today or the Chinese industry tomorrow) will result in an affirmative decision without regard to the treaty requirement of linking significant price suppression to the effects of the alleged subsidy.

35. Regarding the EC’s allegation of pricing matters, as Korea has pointed out and the EC cannot deny, Korean shipyards enjoy a significant cost advantage over the EC. This has been the case for a long time. This advantage has been accentuated in the past couple of years generally by a still weak Won and particularly by the relative strengthening of the Euro compared to the Won. In spite of this, the EC offered a speculative cost model based on unexplained and unproven assertions. Notwithstanding these estimations and assumptions, the EC is trying to make an inference of subsidization based on these speculative projected cost calculations. This would not be acceptable on the part of a domestic authority doing a constructed value determination in an antidumping case; it would be bizarre if used in a countervailing duty investigation and it is wholly unexplained why this Panel in a serious prejudice case should engage in such speculation based on cost modelling and inflation projections that it has not even seen.

36. The EC tries to reassert the abandoned claims of price undercutting. The “evidence” submitted by the EC is factually false. This is illustrated by the Hamburg Sud case where it is shown that the European yard Odense was the price leader. Moreover, it is impermissible for the EC to try to reintroduce previously abandoned claims at this stage. The EC tried to justify this by saying it is not claiming price undercutting as such, but only to support its price suppression arguments. This is mere sophistry. Normally cases are built on interlocking elements of evidence including “one or several” of the factors listed in Article 6.3. The EC rejected that approach and cannot change it, no matter how much it now regrets its earlier decision. Viewing the EC efforts of trying to establish this serious prejudice case on the narrow basis of price depression or suppression due to capacity issues to the exclusion of every other element of proof is like watching an elephant trying to balance on a pin.

37. Even considering that, if the EC’s speculative cost modelling projects a uniform effect across the whole of Korean industry, it necessarily follows that the price effects are not from the alleged subsidies, but are instead from the pricing practices of the majority of shipyards that were not restructured. It is illustrative that the EC continues to claim price leadership by non-restructured yard Hyundai Mipo based on the allegation that Hyundai Mipo has benefited from the APRGs or PSLs. However, Hyundai Mipo had only a very limited number of PSLs and APRGs and the amounts of
benefits (if any) were minimal and certainly by far insufficient to explain the price difference of 15 per cent which the EC alleges with the competing Lindenau offer. (Korea also notes that the EC ad valorem subsidization across its shipyards is much higher and would need to be considered in any proper causation analysis.) That is, the EC’s own approach of lumping everything together based on generic cost/price modelling actually leads to the opposite conclusion of what the EC wishes. Any price effect is not that of the alleged subsidies.

38. One of the many problems here is that the EC is collapsing distinct steps. The treaty text in each of the subparagraphs of Article 6.3 is that the “effect of the subsidy” is to cause one of the possible elements that can be a constituent of serious prejudice. That is, the causation within 6.3(c) is not of serious prejudice, but of the possible supporting factors. The treaty clearly states that the EC must demonstrate that the effect of the alleged subsidies is to cause significant price depression or suppression. There is no dancing around these words. Those specific identified subsidies must be actually having an effect themselves of significant price depression or suppression. Other factors may be at play and they may also have price depressive or suppressive effects, but such effects cannot be attributed to the alleged subsidies. Korea must point this out once again because the EC does not even get to the point of separating out the effect of the subsidies and, instead, tries to rely on the effect of the products. Only then after that element is established as an effect of the alleged subsidy can the complainant move on to show that that one element listed in 6.3 alone or along with others of the several identified elements may be causing serious prejudice. It is axiomatic that other factors causing the prejudice cannot be attributed to the alleged subsidies. This is not only required by the jurisprudence relating to all injury-type inquiries, but it is also mandated by the full contextual analysis of Part III which provides in Article 7.8 that one available remedy is to remove the injury. If there has not been a reliable analysis tracing through from the alleged subsidy having the effect of significant price suppression which, in turn causes serious prejudice, then this analysis is rendered literally impossible.

39. In conclusion, it is clear that the EC has failed to carry its burden of proof, indeed, has misconstrued that burden as a matter of law. Moreover, arguing in the alternative and at the request of the Panel, Korea has adduced substantial evidence on each legal point demonstrating that there is no basis for the EC’s claims. Accordingly, Korea requests that the Panel reject the EC’s claims under Parts II and III of the SCM Agreement.