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Committee on Subsidies and
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REQUEST FOR CONCILIATION UNDER ARTICLE 17 OF THE AGREEMENT

Communication from the Commission of the European Communities

The following communication has been received from the Commission of the European Communities.

The Commission of the European Communities requests on behalf of the European Economic Community that certain issues surrounding the countervailing duty investigation on pasta originating in or exported from the European Community carried out by the Government of Canada be referred to the Committee on Subsidies and Countervailing Measures at its meeting on 27-28 October 1986 for conciliation under Article 17.1 of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade.

Background

On 26 June 1986 the Commission, on behalf of the European Community, held consultations under Article 3.1 of the Code with representatives of the Canadian Government concerning a complaint submitted on behalf of the Canadian Pasta Manufacturers' Association in respect of pasta originating in or exported from the Community to Canada. At the meeting the Commission presented the Canadian representatives with a memorandum¹ demonstrating why there was insufficient evidence as required under Article 2.1 of the Code on Subsidies and Countervailing Duties on all three elements necessary to initiate a countervailing duty investigation, i.e. a subsidy, injury and causal link between them. Consequently, the Commission requested the Canadian authorities to dismiss the petition.

Despite the Community's representations the Canadian authorities decided to initiate a countervailing duty investigation. The preliminary results of this investigation were made known to the Commission and published at the beginning of October and showed that the Canadian Deputy Minister of National Revenue had made a preliminary determination of subsidizing respecting EC exports of pasta to Canada. In the Statement of

¹ A copy of this memorandum is annexed to this document.

Reasons accompanying the Deputy Minister's decision, it was stated also that:

"... Based on updated information provided by the complainant, it is apparent that the elements of injury present at the time of the initiation of this investigation still exist at the present time."

The Community vigorously contests the findings of the Canadian authorities in this case and wishes to refer to and reiterate the points made at the stage of bilateral consultations with the Canadian authorities as outlined in the attached memorandum. In addition, the Community considers it essential to bring to the Committee's attention a number of other issues relating to the unsatisfactory conduct of the countervailing duty proceeding and the lack of any legal basis for imposing measures in this case.

Absence of evidence of material injury

Under Article 5.1 of the Code, provisional measures may be taken only after a preliminary affirmative finding has been made that a subsidy exists and that there is sufficient evidence of injury as provided for in Article 2, paragraph 1(a) to (c). The Commission has already demonstrated in its memorandum that there is no evidence of any material injury being caused to Canadian pasta producers as a result of allegedly subsidized EC exports of pasta and that any difficulties that the producers concerned may be encountering must be due to the restrictions on the purchase of durum wheat imposed on them by the Canadian Wheat Board. In support of this contentions of lack of causality the Commission has shown that Community exports to Canada are small both in terms of quantity and market share.

The Commission is unable to understand why no account has been taken of these facts. In its Statement of Reasons the Department of National Revenue relies solely on allegations made by the complainants and, as described in the Statement of Reasons, these are of such a general and unsupported character as to be virtually meaningless. Statements such as:

"One of the Canadian producers has recently stated that the situation has not improved since the initiation of the investigation."

"A second Canadian producer has confirmed that the competitive situation with Italian pasta has not changed ..."

"A Canadian producer provided distributor price lists showing an Italian brand being offered at low prices."

are totally insufficient bases on which to draw the conclusion that "... the major indications of injury analyzed prior to the initiation are still present and there are reasonable indications that the situation is caused by the subsidized products."

The reliance on mere allegations by the complainants to support the preliminary finding of injurious subsidization constitutes a violation of the requirement under Article 5.1 of the Code that there be sufficient evidence of injury. It is evident, therefore, that no provisional measures should have been taken. However, even if a preliminary affirmative finding of subsidization had been demonstrated, an investigating authority should take provisional measures only if they were necessary to prevent injury being caused during the rest of the investigation. In the absence of any positive evidence of material injury being caused to Canadian producers by EC exports, the Canadian authorities should have refrained from applying provisional measures during the course of the rest of the investigation.

Calculation of alleged subsidization

The Commission wishes to take issue also with the method chosen by the Canadians to calculate the rate of alleged subsidization in this case. Having established an investigation period (September 1985-June 1986) for determining whether subsidization exists the Canadian authorities ignored this period for setting subsidy rates and chose instead to base the rates on the latest data on Community refunds relating to September 1986. It is evidently not a coincidence that the latest date gives the highest subsidy rates. No provision is made either to reduce the subsidy rates if refunds should fall in the course of the rest of the investigation.

The Commission considers that the deviation from the investigation period is in contradiction with traditional procedures of investigation mandated by the Code whereby duties are set on the basis of facts relating to the period of investigation. The arbitrary setting of rates on the basis of facts outside the investigation period, evidently designed to maximize alleged subsidy rates, is not in conformity with the provisions of Article 4.1 which stipulates that the duty should be less than the subsidy if such lesser duty would be adequate to remove the injury to the domestic industry. In selecting an artificially high subsidy rate the Canadian authorities have given added protection to an industry which has not been injured at all.

Conclusion

The Community considers that there is no basis in the Code for the imposition of provisional countervailing duties in this case. Consequently, and for the reasons set out above and in the accompanying memorandum, the European Community requests conciliation on an urgent basis pursuant to Article 17 of the Agreement.

Finally, the Commission wishes to make clear that it has highlighted in this memorandum only certain points relating to this countervailing duty investigation. This does not imply in any way, however, that it accepts the position of the Canadian authorities on other points of principle relating to the case.

Memorandum from the Commission of the European Communities
Concerning the Complaint Submitted on Behalf of the
Canadian Pasta Manufacturers' Association to the
Canadian Department of National Revenue in Respect of
Pasta Originating in or Exported From the European Communities

The delegation of the Commission of the European Communities presents its compliments to the Department of External Affairs and has the honour to refer to the complaint submitted on behalf of the Canadian Pasta Manufacturers' Association to the Department of National Revenue in respect of pasta originating in or exported from the European Communities. The Commission has examined this complaint and wishes to make the following observations.

Conformity of Community restitutions on pasta with the GATT

In the complaint reference is made to the GATT Panel established by the Committee on Subsidies and Countervailing Measures which was set up to examine the dispute between the EC and the United States on the conformity of the Community's restitutions on pasta products manufactured from durum wheat with the dispositions of the Code on Subsidies and Countervailing Duties. The complainants have drawn conclusions and inferences from the proceedings of the Panel which are at variance with the real state of affairs pertaining to the report and its findings. In this context, the Commission would underline that:

- the Panel was unable to reach unanimous conclusions on the applicability of Article 9 of the Code to the restitutions in question;
- the GATT Committee on Subsidies and Countervailing Measures did not agree on the conclusions drawn up by the Panel and the Community was not the only signatory to oppose the conclusions of the Panel;
- in the light of the differences of opinion prevailing in the Committee, the report could not be adopted;
- the Panel report has no legal status nor does it form part in any way of GATT jurisprudence on subsidy matters.

In the light of these factual observations on the Panel report it follows that the argument advanced by the complainants that EC pasta restitutions are GATT-illegal is wholly unfounded.

Do the complainants represent a major proportion of the industry?

Under Article 2(1) of the GATT Code on Subsidies and Countervailing Duties, Canada may normally only initiate a countervailing duty investigation following a written request by or on behalf of an industry, which Article 6(5) of the Code defines as those producers that account for a major proportion of the domestic production of the like product, i.e. pasta.

In this case, there is no indication whether the members of the Canadian Pasta Manufacturers' Association who support the complaint constitute a major proportion of the industry as the GATT Code on Subsidies and Countervailing Duties requires. In this regard it is noticeable that one member of the Association, Gattuso, appears not to support the petition. No indication is given as to the relative importance of this company amongst Canadian producers. The Commission submits that the Canadian authorities should verify that the petition is supported by a major proportion of domestic producers before considering whether to initiate a countervailing duty case against EC exports of pasta to Canada.

Community export refunds

The refunds payable to pasta producers in the Community upon exportation of produce abroad are based solely on the primary product element, i.e. the durum wheat from which pasta is made. The amount of the refund is calculated by reference to the world market price of durum wheat, the benchmark for which is the Minneapolis market price. The Community's mechanism for refunds is calculated in a manner which does not give rise to subsidization of the raw material input at below world market price levels.

It is important in this context to bear in mind that the refund is paid also on Canadian durum wheat imported into the Community in cases where, upon entry into the latter, an import levy has been paid. In instances where inward processing arrangements are applied neither levies are paid nor refunds granted. Italy imported 280,000 tonnes of such wheat from Canada in 1985, 10 per cent of domestic consumption of this product. A proportion of Canadian product would be re-exported in the form of pasta produced in the Community.

Injury

In examining the injury allegedly caused by subsidized imports of pasta from the Community, the Commission would preface its remarks by pointing to the inherent difficulties in making comments on the basis of the limited information contained in the non-confidential version of the complaint. On the basis of the information available, however, there is no evidence of injury caused to the producers. Furthermore, the complainants' assertion that there is a causal link between allegedly subsidized exports of pasta from the Community and injury to producers is wholly unsubstantiated by the information presented.

With regard to the position of the Canadian producers on the market the Commission submits that any difficulties caused to the producers may, in the light of comments made by the complainants in their petition, be due to the operations of the Canadian Wheat Board from whom producers are obliged to buy high cost durum wheat at a premium over market prices (e.g. pages 2, 3, 29 and 46 of the complaint). It goes without saying that in such circumstances Canadian producers may be at a disadvantage when competing with producers who are supplied with durum wheat at world market prices. These disadvantages may be expected to increase if the anticipated

price of durum wheat increases by 57 per cent in August this year, as is anticipated by the complainants. In such circumstances it is hardly surprising that Canadian producers will have difficulty in passing on the cost increases arising from the elevated price paid for the basic raw material input.

If the Canadian producers are suffering injury, it would be expected that their market share would decline and that of allegedly subsidized imports would increase. Far from showing this, however, the data available to the Commission suggests that the Italian share of the Canadian pasta market has remained virtually static between 1983 and 1985 at about 6-7 per cent of total consumption. Whilst it is true that imports from Italy and other non-Community sources rose between 1983 and 1984, the market also expanded significantly in this period. Between 1984 and 1985, however, Italian imports fell by nearly 10 per cent whilst the market increased by about 3 per cent. Taking the period as a whole there is no evidence of an increased penetration of Italian exports on the market.

As regards developments in the first quarter of 1986, Community statistics show that Italian exports of pasta to Canada increased by a modest 8 per cent over the same period in 1985. This official figure needs to be contrasted with the exaggerated claims of a surge in Italian imports in 1985/86 advanced by the complainants. It also disproves the complainants' argument about displaced Italian pasta exports to the United States arriving in Canada in large quantities. An 8 per cent increase in exports in one quarter is hardly evidence of diversion of trade nor of a threat of future injury.

If Canadian producers have suffered injury, which the Commission disputes, this cannot be attributed to the exports from the Community which are small in quantities and have not been rising in terms of market share. The complainants have provided no evidence of any causal link between these exports and any injury suffered by the Canadian producers which, as has been demonstrated, more plausibly emanates from the operations of Canada's internal system for wheat purchases.

In the absence of sufficient evidence as required under Article 2.1 of the Code on Subsidies and Countervailing Duties on all three elements necessary to initiate a countervailing duty investigation, i.e. subsidy, injury and a causal link between them, the Commission concludes that the complaint is unfounded and should be dismissed.

The Delegation of the Commission of the European Communities avails itself of this opportunity to renew to the Department of External Affairs the assurance of its highest consideration.