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GROUP 3(b) - COUNTERVAILING DUTIES

Memorandum by the Canadian Delegation

1. The Trade Negotiations Committee at its meeting on 7 February 1974, decided that a Group should be established to deal specifically with non-tariff barriers. The Trade Negotiations Committee on that occasion also drew up a general programme of "preparatory work of an analytical and statistical nature". This work programme provided that Group 3(b) inter alia should continue the work on export subsidies and on countervailing duties already put in hand in Working Group 1 of the Committee on Trade in Industrial Products.
2. The Canadian delegation thought that other members of Group 3(b) might find it useful if they were to have available to them at this time a memorandum which would describe the nature and extent of the problems which face the participants in this area and which would also set out some of the options as perceived by one delegation. The Group might wish to consider these options if it is considered timely to examine new arrangements, either under the General Agreement or under any other understanding that might be reached in the course of the negotiations, respecting the imposition of countervailing duties.
3. The present memorandum is put forward by the Canadian delegation to assist the Group in its preparatory work on this subject. It is a discussion paper only and should not be regarded as necessarily reflecting the views of the Canadian Government. Nor is it intended in any way to prejudge the scope or content of future negotiations which may be undertaken on these matters in the Trade Negotiations Committee or any other forum.

Problem

4. It is clear that governments in all countries are relying increasingly on incentive programmes to achieve their goals of realizing and enhancing the efficiency of their domestic industries. Some are clearly related solely to export performance, others are designed to support domestic industrial development. In certain circumstances these industrial development programmes may also have significant export

stimulating or import replacing effects. In order to protect themselves against the impact of inflows of subsidized products from other countries which these programmes may give rise to, some countries have enacted legislation to permit their administrative authorities to apply countervailing duties to offset the direct or indirect payments of bounties, grants or subsidies.

5. The key provisions of the GATT covering the imposition of such duties are contained in Article VI. This Article also deals with the imposition of anti-dumping duties. The provisions of the Article, of course, were drafted at a time when there was, generally speaking, less government involvement in industrial or regional development and in economic development programmes generally. The circumstances of today are very different from those envisaged when the countervailing duties provisions of Article VI were drafted. Both for this reason, and because it is clear from recent experience that the application, or threat of application, of countervailing duties can result in dangerous and indeed divisive confrontations between governments, it may be timely to undertake a thorough review of the international provisions governing the application of countervailing duties.

Objective

6. This memorandum attempts to set out some of the considerations that will need to be taken into account in any review of existing GATT provisions. It also examines some of the key elements which would have to be considered in the course of such a review. Finally, it attempts to list - and to examine briefly - a number of options or alternative approaches which might serve as a basis for future discussion in the Group.

Considerations

7. While the provisions of Article VI concern themselves with both anti-dumping and countervailing duties, the two measures are, in reality, quite different. They address themselves to different problems. Article VI:1 defines dumping as a process "by which products of one country are introduced into the commerce of another country at less than normal value of the products". The purpose of anti-dumping duties, therefore, is to deal with the discriminatory pricing practices of individual firms in international commerce. It can, therefore, be conceived as being the counterpart in commercial policy of domestic laws which have the effect of forbidding or controlling the practice of price discrimination in internal commerce. The Robinson-Patman Act of 1936, for example, empowers the Federal Trade Commission in the United States to issue restraining or prohibiting orders to deal with discriminatory pricing practices in domestic commerce. There are similar provisions in the domestic laws of other countries.

8. Moreover, the provisions of Article VI of the GATT (and presumably most anti-dumping systems) do not concern themselves with whether or not the discriminatory pricing practices were facilitated by a subsidy extended by a foreign government or one of its agencies. The essence of the determination as to whether there is dumping is whether or not "the price is less than the comparable price in the ordinary course of trade for the like product when destined for consumption in the exporting country". This is a question of fact about the pricing practice of an individual business enterprise.

9. By contract, countervailing duties are designed to offset assistance provided by governments. Article VI:3 specifically states that the term "countervailing duty" shall be understood to mean "a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly or indirectly, on the manufacture, production or export of any merchandise". Most bounties or subsidies, are, in fact, paid from the public sector; subsidies are payments made by governmental (or quasi-governmental) agencies.

10. It is recognized in the Article, of course, that there may be transactions where both subsidization and dumping exist. Paragraph 5 provides that no product "shall be subject to both anti-dumping and countervailing duties to compensate for the same situation of dumping or export subsidization". The Article, therefore, draws a clear line of distinction between the two concepts. In relation to both types of special duties, there is the requirement that such duties shall not be imposed except when the imports in question are causing or threatening material injury to an established industry or are materially retarding the establishment of a domestic industry. This is presumably the principal reason why the two duties are dealt with in the same Article of the General Agreement.¹

11. Another reason is that in many countries provisions for both types of duties are contained in the same legislation. But the two duties are conceptually distinct. They are designed to deal with different situations: one involves essentially commercial decisions by individual firms to engage in discriminatory pricing; the other addresses itself to a situation in which imported goods may be held to benefit from some subsidy from the government of an exporting country, presumably in pursuit of policy objectives of the government and legislature of that country.

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¹The provisions of the Havana Charter (Article 34) covered both types of measures in the same Article. It may well be that the attempt to deal with both types of situation in the same Article has had, on balance, a perverse effect. Certainly the discussion both in the Working Party on Other Barriers to Trade in 1955 (BISD, 3rd Supplement) and in the Report of the Group of Experts which met in 1959 and 1960, was almost wholly concentrated on anti-dumping duties and the subject of countervailing duties occupied only a few paragraphs at the end of the second report of the Group (BISD, 9th Supplement, pages 200-201).

12. Because of the very real differences between the two measures, members of the Group might conclude that different ground rules and agreed procedures might be needed to regulate the use of countervailing, as distinct from anti-dumping duties. Because the former involves the use of measures by one government to offset or counter measures of another government, a different approach may be required than for anti-dumping duties where the injured party is a particular industry and the remedial measure is directed against an individual firm or firms in other countries. There is no a priori reason, therefore, why solutions appropriate to the international regulation of the use of anti-dumping duties should necessarily be the most appropriate or effective in determining internationally-agreed rules governing the use and application of countervailing duties.

13. It is also clear that the drafters of Article VI had in mind that countries should not resort to countervailing duties without carefully assessing the impact of the imports benefiting from the alleged subsidy. Prior to imposing countervailing duties, contracting parties were required to assess whether or not the imports in question were causing or threatening material injury by reason of their being subsidized. Only in the event that this was established as a matter of fact was the application of countervailing duties allowed. The Group of Experts was quite categorical on this point. In their view it was "essential" that countries should avoid the "immoderate" use of either anti-dumping or countervailing duties. They added that "these duties were to be regarded as exceptional and temporary measures to deal with specific cases of injurious dumping or subsidization".¹ Quite apart from the problems of judgement that arise in respect of determinations of injury in particular transactions and the further problem of ensuring that domestic legislation and administrative practices do accurately reflect what has been agreed internationally, there is the additional difficulty that in respect of countervailing duties, the government of one country, relying on the Protocol of Provisional Application, does not consider itself to be bound by the injury provisions of Article VI. It is understood that the government of that country has applied the provisions of its countervailing duty legislation in response to complaints by firms or associations who

¹BISD, 8th Supplement, page 145.

see themselves being adversely affected by imports of what are considered to be subsidized goods. It is not clear that in all cases the imposition of such duties would have been justified if a material injury test had applied.¹ A meaningful definition of material injury is obviously a key matter for consideration in the course of any negotiations in this area.

14. Agreement on the range and extent of subsidy programmes which are relevant to the rights and obligations now set out in Article VI is also critical. The Article speaks of "export subsidization" and specifies that the maximum amount of duty that can be levied should not exceed "the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product". This definition may be adequate in dealing with transactions in which payment or amount of subsidy is related to the degree or extent of export performance. There is much more uncertainty concerning its applicability in cases where there is no connexion in policy and programme terms between the granting and payment of the subsidy and export performance. The use of explicit or clearly identifiable export subsidies is much less common today, particularly in developed countries, than it was in the years prior to the drafting of the General Agreement. There were a number of classic cases, particularly in the 1930's² of subsidies designed to encourage exports, and presumably these were uppermost in the minds of the drafters when they tried to frame appropriate provisions to permit countries to protect themselves against such practices when they caused or threatened injury to domestic industries. In the last twenty-five years the scope, variety and policy objectives of domestic subsidy programmes have expanded considerably. Subsidies today are used in support of a wide variety of government objectives. These include broad social and economic programmes dealing with such matters as overall industrial development, encouragement of particular manufacturing (or resource) industries, agriculture, regional development, national transportation and manpower training. Governments consider many of these programmes as essential to their countries'

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¹ Authority for the imposition of countervailing duties in the United States is contained in Section 303 of the United States Tariff Act of 1930. Since the legislation predates the General Agreement, the United States Government has taken the position that it is not required to adhere to the injury provisions of Article VI. In some recent cases, notably the action against imports from the Michelin Tire Manufacturing Company of Canada, it is doubtful that material injury or threat of material injury could have been established in view of the small proportion of the United States market for tyres which might have been taken by imports from Michelin.

² See G.A. Elliott, Tariff Procedures and Trade Barriers - University of Toronto Press, Toronto, 1955, p. 174, and DISD, vol. IV, Annex I, Ad Article VI, re multiple currency practices.

economic development. Some of these programmes undoubtedly have an effect on international trade, whether it be on imports or exports. Few of them, however, are linked directly or indirectly, to the achievement of particular export or import replacement targets. But there are probably few goods moving in international trade today that have not benefited in one way or another from government assistance. If virtually all goods are subsidized then the key question is what types of subsidies should occasion the possible use of countervailing duties? On this, Article VI is quite explicit: it is only those subsidies defined in that Article and that give rise to injury that can properly be offset by a special duty.

15. Finally, because the application of countervailing duties by one country is specifically designed to counter the impact of another government's programmes, there is considerable scope for conflict between governments. In many cases where countervailing duties are imposed both governments may be subject to domestic political pressures to take offsetting actions, and thus the danger of misunderstanding and escalation of the dispute can be very real. Members of the Group may wish to examine, therefore, whether there should be new arrangements for consultations between governments and whether such arrangements might assist in avoiding the unnecessary use of countervailing duties.

16. The above considerations suggest that there are a number of questions which merit fuller examination before any attempt is made to decide on the form of any new commitments or understandings with respect to the application of countervailing duties. The problems which seem to warrant careful consideration by the Group may be subsumed under three headings:

- (a) Questions related to the concept of material injury.
- (b) Range of subsidies to be covered.
- (c) Provisions for consultations between governments.

Material injury

17. Reference has already been made to the importance which the drafters of Article VI and subsequently the Group of Experts attached to the requirement for an injury test. The question arises whether the existing provisions are sufficiently precise. It was the view of the Group of Experts in 1959 that it was not possible to arrive at precise definitions or sets of rules.¹ In drawing up the Anti-dumping Code, the participants felt a need to try to specify more precisely what was intended. Article 3 of the Code provides that a determination of injury shall be made only when the "dumped imports are demonstrably the

¹BISD, Eighth Supplement, p. 150.

principal cause of material injury" and that the evaluation of the effects of the dumped imports on the industry in question shall be studied by reference to the important (and obvious) indices of the economic activity of an industry. There is no definition of injury as such or of the adjective material.

18. Experience since the adoption of the Code demonstrates that fundamental differences exist between governments with respect to case and frequency with which injury or threat of injury is found, especially those governments that use their anti-dumping legislation most extensively.¹ It has not been possible to reach any significant measure of agreement on these matters in the GATT Anti-Dumping Practices Committee. The Group may, therefore, want to consider whether any agreement may be required to ensure a broader measure of understanding on the meaning of the injury provisions of Article VI and a commitment by the participants to make determinations of injury in a meaningful and more nearly uniform way in respect of the use of countervailing duties.

19. Associated with the general definition of injury are questions concerning what effectively constitutes an "industry" and a "regional market". Both are important in assessing whether or not imports are injurious in a given instance. Here again the Anti-Dumping Code attempted to achieve a greater degree of precision. Article 4 says that the term "domestic industry" shall be interpreted as referring to the domestic producers as a whole or those whose output constitutes "a major proportion of the total domestic production of the like products", but in exceptional circumstances (as described) a country may be divided into two or more competitive markets and the producers in each market regarded as a separate industry. Both concepts have proved difficult to interpret and, in some instances, have been applied in very restrictive manner by some signatories to the Code.² Here again there is clearly room for improvement with respect to the application of these terms in any understandings which may be reached regarding the use of countervailing duties.

20. Finally, the question has been raised from time to time as to whether or not there should be quantitative thresholds or minima respecting the magnitude of the increase in imports or their impact on domestic employment or production as measured by the sorts of indices noted in the Anti-Dumping Code. It has also been suggested that there should be some ranking in importance of the various criteria set out in Article 3 of the Anti-Dumping Code. Members may wish to consider whether it would be advantageous to set thresholds or to provide for a

¹In one recent case in the United States threat of injury was found even though the product in question was in short supply and the effect of levying anti-dumping duties on imports was likely to reduce imports and hence accentuate shortages and price pressures. See letter of 27 March 1974 from Chairman of Cost of Living Council to the Chairman of the Tariff Commission re lead imports from Australia and Canada.

²See Rodney de C. Grey, The Development of the Canadian Anti-Dumping System, Private Planning Association of Canada, 1973, pages 44-49.

ranking of criteria. If so, it would also be necessary to find some method of reaching agreement on the appropriate ranking and thresholds.

21. Members of the Group would also want to consider whether such threshold levels would come to be regarded as trigger points and, thus, the new international agreement would have the perverse effect of bringing about virtually automatic injury determinations whenever the minima were determined to be met. The question is whether greater precision will be worth the price.

Subsidies

22. There has been comparatively little discussion in the GATT as to what constitutes a subsidy liable for countervailing duties action under Article VI:3. The point has been made above that governments today use a wide variety of subsidy measures, few of which are clearly linked to export performance but which, nonetheless, often have a significant impact on imports or exports.¹ Therefore, the question is whether the term "subsidy" in Article VI:3 should be given a broad or a narrow interpretation for purposes of the application of countervailing duties or of whatever arrangements may be agreed upon in this connexion. The subject clearly requires much more detailed consideration.

23. The Group of Experts were not able to agree as to whether "subsidies" covered only those that had been granted by governments or semi-governmental bodies. Some felt that the term should also cover bounties and grants by private bodies.² Participants may wish to consider this question again.

24. There is no clear understanding among contracting parties about the relationship of Article VI to Article XVI of the GATT. Article XVI deals with subsidies in a more general way. It was the view of the Group of Experts, however, that the fact that certain subsidies were permitted under Article XVI "clearly did not debar importing countries from imposing a countervailing duty on the products on which subsidies had been paid".³

¹This is clearly more likely to be so in a country where imports and exports account for a large proportion of the gross national product. Thus, the impact on imports and exports is likely to be larger if the country concerned is small relative to its principal trading partners. For these countries a small increase in the percentage of national production exported by the larger country could correspond to a major increase in imports in the smaller country. Similarly, the smaller country, because of the limited size of its domestic market will export a high proportion of its domestic production. The overall impact on the imports of the larger country, however, may be minimal.

²BISD, Ninth Supplement, page 200

³Ibid

25. Finally, the suggestion has been made by one member that countries should be permitted to apply countervailing duties without an injury test to offset any one of an agreed list of prohibited subsidies. It has also been suggested that this list include all export subsidies and certain other domestic subsidies which have export-stimulating effects. Other participants would argue that equal attention should be given to subsidies having import replacing effects. The Group would, of course, need to consider this proposal in more detail if it was to take the proposal under consideration. In view of the difficulties of reaching agreement in the GATT preparatory work on an indicative list of export subsidies, it would appear that participants would likewise experience difficulty in reaching agreement on such a list even if it was to be confined to export subsidies proper.¹

26. No matter how comprehensive the list might be, countries might find other ways of maintaining their competitiveness, especially if the impact on the international flow of goods of particular measures could be regarded as being incidental to the domestic objective for which the subsidy had been granted.

Consultation

27. Article VI does not specifically provide for consultations prior to the imposition of countervailing duties. In the Group of Experts, however, the majority were of the view that it would be "normal, and at least desirable" if a country planning to impose countervailing duties were to "enter into direct contact with the government of the exporting country" in order to arrive at an estimate of the amount of the bounty concerned.

28. On the broader issue of consultation, it was the view of the drafters at Havana that no special consultative machinery was necessary and that the general provisions of Article XXII and XXIII were adequate to meet any concerns about abuses to the levying of countervailing duties. An important example of recourse to these provisions is the Article XXII consultations which the Canadian authorities are conducting with American authorities respecting the application of United States countervailing duties in the Michelin Tire case. There are, of course, provisions for consultations under Article XVI:1. Such consultations are not intended to address themselves to the question of whether or not

¹It will be recalled that the Panel set up in 1959/61 decided inter alia that "it was neither necessary nor feasible to seek an agreed interpretation of what constitutes a subsidy". BISD 10th Supplement, page 201.

countervailing duties are appropriate but rather the intent is to enable the country affected by the subsidy practices of another to seek consultations if there is "serious prejudice" to its interests. In practice, however, these consultation provisions have been largely ignored.

29. It is for consideration whether broad provisions for consultation similar to those contained in Article XVI:1 should be imported into Article VI or into any new GATT provision or article dealing with countervailing duties. Indeed, participants may wish to consider whether before imposing countervailing duties or other offsetting measures governments should be required to consult with the government of the country alleged to be granting the subsidy, and perhaps to examine the issue with a multilateral surveillance body. Such consultations would cover the magnitude of the alleged subsidy, its impact on international trade, the objectives of the governments concerned, and the possibility of other methods less damaging to trade being found to achieve these objectives. Obviously such consultations should not be limited to subsidies which affect exports against which countervailing duties provide a remedy, but should also cover subsidies which distort trade by encouraging import replacement.

Alternatives

30. Apart from considering some of the key questions above, members of the Group may also want to examine the various ways in which the Group can proceed and the options open to them. There are a number of alternatives:

1. Development of a code governing the application of countervailing duties.
2. Preparation of a Declaration or Interpretative Note expanding on particular provisions of Article VI as they apply to countervailing duties.
3. Agreement on new bilateral consultative procedures reinforced by multilateral surveillance provisions.
4. No change in the existing provisions or procedures under Article VI but perhaps a tightening up of the present provisions of Article XVI respecting subsidies.

5. A new article of the Agreement dealing with measures which may be used to offset export subsidies or subsidies for import replacement.

6. Some combination of the foregoing alternatives.

Some elements of these alternatives are examined below.

A Code

31. In earlier discussions it was suggested that an attempt should be made to negotiate a code governing the application of countervailing duties.¹ This, in the view of some, would correspond closely to the Anti-Dumping Code. It would appear on closer examination that the two Codes would bear very little resemblance to one another, except perhaps with regard to the definition of material injury. It has been suggested that a Code might provide for virtually automatic application of countervailing duty, without a test of material injury, to goods which have benefited from a subsidy which the authorities in the importing countries deem to be prohibited under Article XVI. Such a code would not be in accord with Article VI; moreover it would involve the concept of one country determining unilaterally that another country was in breach of its obligations and unilaterally applying a sanction. Such a concept is quite foreign to the GATT, and the dangers inherent in it are obvious.

32. It would also be necessary to decide whether or not a Code should also contain provisions similar to those in Article VI:6(b) and (c) respecting the imposition of countervailing duties by a member to assist in cases where subsidized exports were causing or threatening material injury to a third country and, if so,

¹The idea was discussed during the preparation of the Anti-Dumping Code and it was subsequently agreed at the twenty-fourth session of the CONTRACTING PARTIES that a working party should be set up to study "countervailing duties, subsidies and other export incentives". The working party was never established. However, the question came up again during discussions in the Committee on Trade in Industrial Products, and it was agreed that the terms of reference of Working Group 1 of the Committee should be broadened to include countervailing duties and subsidies. A background note on these matters was subsequently issued by the secretariat (COM.IND/W/98 dated 14 March 1973).

whether these provisions are adequate or require further definition. There is the further question as to whether all participants would agree to adhere to a Code and, if not, whether those that adopted the Code would be governed by its provisions in their treatment of imports from other countries, whether or not they were signatories of the Code.¹

33. It would be necessary to consider what provisions, if any, should be envisaged for effective surveillance and whether or not sanctions should be provided in the event that members of the Code did not adhere to their obligations.

34. The Group may wish to consider whether in any Code it might be appropriate to ensure that domestic legislation should not require governments to initiate countervailing duty investigations automatically on the receipt of a complaint from a firm or association. Both subsidy programmes and the offsetting measures that can be taken against them involve the actions of governments not the actions of enterprises. The decision as to whether or not action should be taken in a particular case should remain the prerogative of governments.

Declaration or Interpretative Note

35. A less ambitious undertaking would involve trying to reach agreement on one or two of the key issues surrounding the application of countervailing duties without attempting to reach a comprehensive understanding on all elements that might be contained in a Code. This would take the form of a Declaration of Intent or of an Interpretative Note accompanying Article VI. Again the key questions would be a clarification of what would constitute a meaningful test of injury and what types of subsidy should be subject to countervailing duty action. There might also be some emphasis on the need for consultation between governments before action was taken.

Consultative Arrangements

36. Because of the danger of conflict and the escalation of commercial policy disputes between governments, provisions for mandatory bilateral consultations (and perhaps multilateral surveillance) prior to imposition of countervailing duties might well be considered by the Group. Such consultation should go

¹This question did come up in the context of the Anti-Dumping Code. At the twenty-fifth session the Director-General advised that adherents to the Code should apply its provisions on a most-favoured-nation basis, i.e., that all contracting parties to the GATT should be treated the same whether or not they had adhered to the Code.

beyond the 1960 recommendation of the Group of Experts that countries consult regarding the magnitude of the subsidy, and hence the level of countervailing duties to be applied. Consultation should also cover a variety of other issues, such as a review of the evidence of the degree of injury caused or threatened, the nature of the subsidy, the planned duration of the subsidy programme, the objectives of the programme and the impact on trade. The parties might also examine whether other policy devices might be found which would reduce or eliminate the trade distorting effects of the subsidies while permitting achievement of the same general policy objectives. This would be particularly important in regard to import replacing subsidies which, of course, would also have to be dealt with under any new consultative arrangements.

37. It would be necessary to consider carefully the terms of reference and the composition of any multilateral surveillance body. Should it be modelled on the GATT Anti-Dumping Practices Committee which meets once a year and reports to the Contracting Parties on how the Code is being administered by its adherents? The deliberations of this Committee have not had great impact on the practices of governments applying anti-dumping duties. Or should it be similar to the Textiles Surveillance Body which has been established to supervise the implementation of the recently concluded GATT Arrangement Regarding International Trade in Textiles and to consider complaints by individual members who feel they have not received satisfaction under the Agreement? Again, a judgement would have to be made as to whether non-adherents would have access to such a body if they judged themselves to have been unfairly treated by one of the adherents.

Article XVI

38. Finally, it has been suggested that the nub of the problem is the prevalence of export subsidies rather than the use of countervailing duties and that the focus of attention should be on more carefully defining what are export subsidies and deciding what, if anything, should be done about them. It would follow that attention should be directed to Article XVI - not Article VI. The difficulty with this approach is that export subsidies are only a part of the more general

¹Once again there would be little point in such understandings unless they were subscribed to by at least all the major trading countries and particularly those most likely to resort to the use of countervailing duties.

subsidy issue dealt with in Article XVI. Moreover, even if an attempt were made to reach agreement within the context of Article XVI as to what should be done about subsidies in general and export subsidies in particular, the issue would remain whether the provisions of Article VI were adequate to the circumstances of today.

39. The Brazilian delegation has submitted for the consideration of this group, a paper addressed to the special concerns of developing countries in the negotiations relating to subsidies and countervailing duties. We should of course take full account of the special interests of developing countries throughout the negotiations but the determination of what differentiated measures, if any, might be appropriate should be done in the light of solutions developed in the negotiations. It might well be that adequate provisions for scrutiny by the CONTRACTING PARTIES of alleged subsidies, and the working out of adequate provisions regarding the test of material injury would make unnecessary any special provisions regarding the exports of developing countries.