

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

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Negotiating Group on Subsidies
and Countervailing Measures

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CANADIAN STATEMENT TO NEGOTIATING GROUP
ON SUBSIDIES AND COUNTERVAILING MEASURES
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Several delegations have made submissions to this Negotiating Group during the past year. While these submissions have addressed both general questions relating to fundamental objectives for the Negotiating Group as well as more specific, technical, points associated with subsidy/ countervail issues, the main focus has been on the latter. Canada welcomes the opportunity at this stage in the negotiations to concentrate on the question of fundamental objectives and the direction and dimension of the negotiations before entering into discussions of specific improvements to the existing rules regarding subsidies and countervailing measures. Without a common understanding of the fundamental objectives of Articles VI and XVI and agreement on the overall direction of the negotiations we are concerned that it will be difficult to make substantive progress on the technical issues.

These comments fall into three parts: first, an analysis of the purpose of Article XVI which relates to subsidies; second a discussion of countermeasures, including Article VI; and finally, some general comments on how these two Articles can be tied together.

Subsidies

Articles XVI deals with subsidies and the desirability of containing their use where they cause prejudice to the interests of contracting parties. This Article was included in the original GATT Agreement in recognition that regardless of the legitimacy of subsidies, they had significant potential to distort trade. As trade barriers fell, governments might resort to subsidization as an alternate means of providing direct protection to domestic industries and promoting import substitution. Subsidies might also be used to increase exports with potentially harmful effects for both importing and other exporting contracting parties. Finally, it is clear that subsidies can affect patterns of investment and result in a misallocation of resources from their most efficient use. It was recognized that subsidies can subvert the GATT objective of liberalizing trade.

At its core, Article XVI reflects an underlying desire to discipline the use of subsidies and to reduce the potential for distortions in the market that can result from their use. But governments were unwilling to accept many limits on their activities, and the obligations fall far short of the desire. The problem over the years has been that elaboration of the self-discipline contemplated in Article XVI has not led to meaningful results for any but certain export subsidies.

Originally, Article XVI provided only for notification and consultation. The consultation clause provides for discussions in the event of actual or potential serious prejudice with a view to limiting the subsidization. The Article was expanded in 1955 with the addition of Part B dealing with export subsidies. Part B contains two major components: a general prohibition of export subsidies on non-primary products and an admonition against the use of export subsidies on primary products.

The work towards expanding disciplines and giving substance to the prohibitions on export subsidies has been positive and significant. However, experience has shown that subsequent efforts to clarify the rules associated with Article XVI, particularly with respect to subsidies on primary products and domestic subsidies, have not been effective in achieving the fundamental objective of limiting the use of subsidies which prejudice the interests of other parties. This has been particularly demonstrated in the area of agricultural subsidies.

Section A of Article XVI provides that in the case of a determination of serious prejudice the extent of the obligation of the subsidizing party is to discuss the possibility of limiting the subsidization. There is no obligation to do anything to correct the situation regardless of the impairment of benefits paid for in previous rounds. Is that equitable?

In recent years we have seen examples of major and wealthy private companies exploiting the natural desire of governments to maintain and attract investment and employment. These companies trigger subsidy-bidding wars in which the pyrrhic prize goes to the deepest pockets but the company reaps the financial reward. The treasures of even the richest must feel the pinch. Do we want this game and can we afford it? Self-interest suggests that it is difficult to move independently, but together we may have possibilities. Some countries have disciplined export credit competition, is there a lesson here?

We have seen situations recently in which subsidies have been used to support domestic production and to displace imports with direct impairment of tariff concessions. Is that consistent with the trade liberalization objective of our negotiating rounds?

The 1955 amendments recognized that the discipline envisaged on the use of subsidies may not meet the intent of the Agreement and made explicit provisions (paragraph 5 of Article XVI) for periodic reviews of the Article to examine its effectiveness. That opportunity was seized in the Tokyo

Round where efforts were made to clarify the subsidy rules by writing the Subsidies/Countervail Code. However, these efforts have met with only limited success. We are here again in Geneva struggling, in part, to deal with the problems caused by subsidization and the need to review and improve the rules.

As called for in Article XVI:5, it is important that we renew these efforts, keeping in mind that Article XVI was written to promote the trade liberalization objectives of the GATT and to avoid seriously prejudicial subsidization. The ground for trade irritants and dispute in this area is already very fertile and holds the unwelcome promise of even more heated friction. We must anticipate this potential friction and engage co-operatively in a determined effort to give meaningful definition to Article XVI. Failure to deal with this fundamental issue has consequences which none of us will be able to avoid but which we know could be very disruptive to the stability of world trade.

Countermeasures

There are two major types of recourse in response to prejudicial subsidization. The first involves dispute settlement and addresses situations where subsidies affect exports to third countries, replace imports, or where a practice is inconsistent with the rules. This type of recourse, however, has proven ineffective in constraining prejudicial subsidization.

The second major type of recourse involves countervail actions to protect domestic producers from injury caused by subsidized imports. This is the fundamental purpose of Article VI. However, it only deals with problems at the border and after the damage has been done. The use of countervail has also given rise to a large number of problems which continue to plague us. The problems arise primarily because there is no general agreement regarding what constitutes a countervailable subsidy, how to measure it, and how that subsidy causes material injury. This lack of agreement has led to unilateral interpretation of rights and obligations in these areas and a great deal of friction. Countervail is a blunt instrument: it is discriminatory in application, it is not subject to compensation, and there are no rights of retaliation. Because of its unilateral application and the absence of clear rules and constraints on its use, it can and has been used as a mechanism of protectionism rather than a justifiable means to protect against injurious subsidization.

Comments

It is clear that the subsidies/countervail system, as embodied in the Subsidies/Countervail Code, is not achieving the fundamental objectives of Articles XVI and VI. There continues to be massive subsidization by governments across a broad range of sectors, including agriculture. It is argued by some that this costly system has not proved particularly effective. Expected employment and income gains may not be realized, permanent, or worth the cost. For example, subsidies are frequently used

to prop-up inefficient industries rather than to encourage real structural adjustment. They are used to maintain or increase production in the face of declining markets and prices and lead to disruptive commodity surpluses in the name of income protection instead of direct income support. Perhaps we should individually reflect on the benefits of these programmes as we consider our willingness to accept disciplines on the instrument.

There is continuous friction over the taking of countervailing duty actions with frequent questioning by the affected country of the justification for such actions. The use of countervailing duties as a mechanism to control subsidization is not likely to be any more effective in the future than it has in the past. First, governments are frequently willing to take the risk associated with the threat of countervail rather than stop subsidizing. Second, the effectiveness of countervail is limited because it does not deal with some of the fundamental trade distortions caused by subsidization: subsidized goods entering third markets and the displacement of imports by subsidized domestic production.

What do we want to achieve on subsidies and countervailing measures in this Round? Let there be no illusion that we can hope to make progress on new disciplines for one without similar progress on the other. If we are not prepared to move beyond paragraph 1 of Article 11 of the Subsidies Code which states that we "do not intend to restrict the right of signatories to use such subsidies" I question whether we have a basis for a negotiation. The maintenance of flexibility on subsidies in the Tokyo Round was largely responsible for the continued capacity for unilateral interpretation of what is countervailable and how. Is that good enough for this Round? The number of demands for changes to countervail suggest that it is not.

Then, there is need to accept meaningful new disciplines on the use of subsidies, not just with regard to subsidies affecting exports but also those domestic subsidies which deny imports the opportunity in a market for which access has already been paid. Apart from countervail, these disciplines are necessary if we are to meet the fundamental objectives of Article XVI. This does not necessarily mean a prohibition of subsidies, but it does imply that there must be clearly designed rules on the use of subsidies to limit their trade distortive effects. Clearer rules should also make it easier to resolve disputes when they arise.

Increased disciplines on subsidies should make it easier to improve the countervail rules and help to prevent countervail from being used to harass or as a protectionist tool. In this regard, we will need to ensure that the fundamental objective of Article VI is adhered to in these negotiations, i.e. that countervail is only to be used in legitimate cases where there is clear evidence of subsidization and resultant injury.

Both Articles XVI and VI were intended to constrain the unilateral rights of governments to act in ways that inhibit trade liberalization. For various reasons we have been unwilling until now to turn those constraints into firm obligations. A balance will have to be struck if we are to be successful. Hopefully, we can reach consensus on the fundamental overall goals and objective of these articles which will pave the way to substantive results in these negotiations.