

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

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Group of Negotiations on Goods (GATT)
Negotiating Group on Subsidies
and Countervailing Measures

FRAMEWORK FOR NEGOTIATIONS

Communication from Canada

Introduction

The Framework for Negotiations approved by the TNC calls for the conduct of negotiations on subsidies and countervailing measures to be guided along the lines of:

- prohibited subsidies
- countervailable/actionable subsidies
- non-countervailable, non-actionable subsidies
- special and differential treatment for developing countries
- notification and surveillance
- dispute settlement.

The Negotiating Group should work toward an agreement that is balanced as between the major components.

We recognize that this submission may cover some elements which are also under discussion in the Negotiating Group on Agriculture but it does not prejudice their contents nor the primary locus of the detailed negotiations.

This submission is not intended to prejudice the form of an eventual agreement. Reference is made to existing rules and to work done under Committee auspices for the purpose of providing a basic reference point for improvements.

Section 1: Prohibited subsidies

Some subsidies have long been recognized as particularly harmful to an open international trade system. The rules and disciplines of the GATT and the Code reflect international consensus that certain of these subsidies ought to be prohibited. Current negotiations should aim at improving, extending and further refining GATT rules and obligations including enforcement with respect to prohibited subsidies.

(a) Export subsidies

The prohibition on export subsidies in the GATT and Article 9 of the Subsidies Code could be strengthened through certain changes.

Extension to all primary products

The prohibition on export subsidies on products other than certain primary products should be extended to include primary agricultural, fish and forest products in their natural forms or which have undergone such processing as is customarily required for international trade. In effect, the artificial distinction between primary and non-primary products in the Code should be discontinued.

Clarification to Illustrative List of Export Subsidies

For example:

Export incentive effects through indirect tax rebate or import charge drawback systems can also constitute export subsidies. The Committee has already adopted guidelines, prepared by the Group of Experts on the Calculation of the Amount of a Subsidy, relating to substitution drawback systems. The List should therefore be amended to provide greater clarity in the operation of this provision (items (h) and (i)).

Export credit guarantee and insurance programmes that do not cover their long-term operating costs clearly constitute a subsidy on exports. The requirement for cost recovery should be strengthened, and there should be agreement on the time-period over which to assess long-term operating costs (item (j)).

Conversion to a definitive list

In order to facilitate the enforcement of obligations, and to reflect the substantial measure of agreement on the functioning of the Illustrative List to date, signatories should agree on the definitive nature of the List. The existing List, with the modifications and additions suggested above, should be entitled simply "List of Prohibited Export Subsidies". In effect, through the amendments suggested here, we will have achieved a more operationally effective definition of export subsidies. A violation of the List would then clearly constitute a prima facie case of nullification and impairment and give rise to specific rights outlined below in the section on remedies.

(b) Other trade-related subsidies

Subsidies that are contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods or upon export performance clearly constitute trade-distorting subsidies. Experience with existing GATT obligations and precedents suggests that these practices should be made subject to an explicit GATT prohibition.

(c) Domestic subsidies

Current rules, while recognizing the legitimacy of various domestic subsidies, also recognize that these subsidies can have adverse effects on the interests of other countries. The only effective discipline on the

possible effects of domestic subsidies on exports is presently through the exercise of countervailing measures, which cannot address import displacement and effects in third country markets.

As a complement to the prohibitions on export subsidies and other trade-related subsidies, the Negotiating Group should aim to strengthen and give greater substance to disciplines on domestic subsidies. This could be achieved in a number of different ways. Participants could explore disciplines on domestic subsidies in terms of overall subsidization, or normative rules on specific types of subsidies, or through multilateral sectoral undertakings.

(d) Remedies - prohibited subsidies

The appropriate remedy for any violation of a prohibition should be recourse to GATT dispute settlement procedures and multilaterally sanctioned remedies.

Procedures should be established to provide for requests from signatories for multilateral rulings on whether another signatory is using a prohibited subsidy. If there is an affirmative ruling, the offending country should withdraw, amend or otherwise bring the measure into conformity with the rules as soon as possible in order to reduce to a minimum any adverse effects. The offending country could also be required to provide compensation for any adverse effects resulting from subsidies which are found to be in violation of the prohibition obligation but which have already been delivered. In the event that withdrawal or amendment does not occur within a reasonable time, there would be provision for the affected country to take effective countermeasures against a prohibited subsidy.

Countries should be able to make references to a multilateral body for an advisory opinion on whether a proposed programme would be considered a prohibited subsidy before the programme is finalized and implemented.

The nature of the remedy available should be restricted to the imposition of increased duties, equivalent to countervailing duties, applied against exports from the subsidizing country. In the case of a prohibited subsidy with adverse effects in the importing country, the duties would be applied to the subsidized imports, while in cases of adverse effects in third country markets or in the home market of the subsidizing country, the duties would be applicable against other goods exported by the subsidizing country to the complaining country (or countries).

Section 2: Countervailable or otherwise actionable subsidies

There is a lack of precision in the General Agreement and the Code on what subsidy practices should be subject to countermeasures. This has led to uncertainty regarding the potential for countervail and opened the door to possible protectionist effects, including procedural harassment of legitimate exports. Strengthened multilateral rules on the use of countervail would enhance the stability and predictability of international trading conditions.

(a) Conditions for countervailability

The concept of specificity should be enshrined as a condition for countervailability. Guidelines for the application of this concept have been pursued in the Committee and could involve:

- the existence of restrictions or exclusions placed by the granting authority which have the effect of limiting access to a subsidy to a particular enterprise or industry, or a group of enterprises or industries, within the jurisdiction of the granting authority; or
- the absence of neutral eligibility criteria, clearly spelled out in law or regulation and capable of verification, on the basis of which assistance is made available.

Predictability could also be enhanced by agreement on the treatment of particular types of subsidies for the purposes of determining countervailability. For example:

- Government provision of equity capital should not be considered a subsidy if shares are purchased at market prices, or, where there is no market price for the shares, if a reasonable evaluation made at the time of the investment decision concluded that the equity would achieve an adequate return.
- The amount of subsidy implicit in a government loan, loan guarantee or loan insurance programme should be measured as the difference between the interest rate charged under the programme and the comparable interest rate that a private sector lender would charge for the same loan in the absence of the programme. In no case should the amount of the subsidy measured exceed the principal amount of the loan made under the programme.
- Where a comparable private sector interest rate cannot be ascertained, the amount of the subsidy may be measured as the difference between the government's borrowing rate and the rate charged on loans made under the programme.

GATT practice and disciplines on subsidies reflect a general view that subsidies exist where the price mechanism is affected by the exercise of government authority to impose tax and to expend revenue, whether directly or through delegation of authority. Current rules apply to practices which involve a direct transfer of funds, potential direct transfers or liabilities, and foregone revenue.

Accordingly, building upon current rules, a basic condition for countervailability of a given measure should be the existence of a financial contribution by government. This condition would be consistent with the objective of offsetting the effects of interference with the operation of the price mechanism.

The conditions under which input subsidies are potentially countervailable are not spelled out under existing rules. It should be made clear that indirect subsidies would be countervailable only to the extent that they meet the following sequence of three tests:

- (i) whether there is pass-through of a subsidy on an input i.e. the input purchase price is less than the prevailing domestic market price or the price the purchaser would otherwise pay for imported inputs;
- (ii) whether such pass-through is specific in nature; and
- (iii) whether the input subsidy itself is specific.

Methods of calculation of subsidies for the purpose of countervail could be clarified, building upon earlier work by the Group of Experts, as follows:

Amortization and depreciation procedures should be followed to allocate the amount of a subsidy over time (a) in the case of a subsidized loan, loan guarantee or loan insurance, over the life of the loan itself, or, (b) where a grant or a loan, loan guarantee or loan insurance, is used for the acquisition of physical assets, over the average useful life of the assets so acquired.

(b) Trade effects - tests for actionable subsidies

(i) In the market of the importing country

The determination of the injurious effect of actionable subsidies is a matter of considerable uncertainty under existing rules, particularly Article 6 of the Code. Greater certainty could be provided by a requirement that the following principal factors be present in order to demonstrate that increased subsidized imports are causing or threatening to cause material injury or retardation: either price suppression or lost sales; and reduced profits. In addition, investigating authorities should take into account the margin of subsidization in determining the existence of injury.

A de minimis standard should be applied to preclude the application of countervailing duties in cases where the amount of the subsidy is less than x per cent of the unit value of the imported goods.

The cumulation of different sources of imports in countervailing duty investigations can lead to the inclusion of countries whose exports contribute to neither injury nor the threat of injury. The capacity to exclude such countries from the scope of a countervailing duty investigation should be strengthened. Accordingly, a permissive clause could be created which would require that cumulation not be mandatory, and that a country may be excluded from the scope of an investigation at any stage, in any case in which imports of the like products from that country are negligible and have no discernible adverse impact on the domestic industry.

Where the domestic industry in a countervailing duty investigation is itself receiving government subsidies, the effect of imposing a countervailing duty on subsidized imports may be inequitable and may increase the degree of trade distortion. This is all the more probable where there is a high degree of openness and economic integration between the importing and exporting countries. In order to establish greater symmetry of discipline, the determination of the amount of the subsidy should be based on the difference between the subsidy on imports and the subsidy on domestic production of the like products.

The domestic industry, in making a petition for initiation of a countervailing duty investigation, should be required to state the amount of any subsidies it has received or is receiving. The exporting country would also have the right to bring forth verifiable evidence of subsidization of producers of the like products in the importing country. The investigating authorities would be required to subtract any subsidies received by the domestic industry before deciding on whether or not to levy a countervailing duty and no countervailing duty should be levied in excess of the difference between the subsidy on imports and the subsidy on domestic production of the like products.

(ii) In the market of the subsidizing country or in third country markets

The purpose of countervailing duties is to remedy injurious trade distortions. However, present rules do not adequately address trade distortions that may occur as a result of subsidies that displace imports in the home market of the subsidizing country or in third country markets. Discipline could be exercised on subsidies affecting the home market through a special nullification and impairment mechanism. For example:

- Any actionable subsidy in excess of a certain maximum level of subsidization could be deemed to constitute a prima facie case of nullification and impairment, unless the subsidizing country could demonstrate otherwise to a multilateral panel. This level would realistically need to be established through negotiation.
- Any signatory that has a substantial interest would be able to invoke this mechanism. A multilateral panel would be required to determine whether the maximum level had been exceeded, and, in the event the offending subsidy is not withdrawn or modified, on the amount of appropriate compensation/retaliation.
- Subsidization below the maximum level would not constitute prima facie nullification and impairment but would continue to be subject to the normal disciplines (i.e. the affected country would continue to have the right to bring forward evidence to demonstrate actual nullification and impairment).

(c) Remedies - countervailing duties

For the purpose of clarifying the scope and transparency of investigative procedures regarding countervailing duties against actionable subsidies, a number of technical but important issues should be addressed. These should include the definition of industry, the standing of petitioners, a sunset clause, and the use of undertakings.

The definition of industry under current rules has resulted in situations where the market structure of particular industries, and the particular nature of trade in the agricultural sector, could preclude the application of countervailing duties even where subsidized imports are shown to be directly causing injury. Accordingly, special provision could be made for clarifying the term "domestic industry" in instances where, by virtue of the particular market structure of an industry based on agricultural inputs, injury caused or threatened by imports of partly or minimally processed agricultural products can be transmitted to producers who have a coincidence of interests in respect of imports of those products and are situated along the same chain of production.

The requirement that the domestic industry in an injury examination constitute a major proportion of the domestic production of like products should be strengthened. The investigating authorities should be required to verify the standing of petitioners, i.e. that they satisfy the major proportion requirement, before initiating investigations. In addition, the requirement could be defined with greater precision, for example in terms of x per cent of total domestic production.

Countervailing duties are subject to a sunset clause under the laws of an increasing number of countries, reflecting the fact that the circumstances of injury caused or threatened by subsidized imports can change over time. The principle of time-limits on their application could be more firmly established by requiring that countervailing duty findings lapse automatically unless a review is conducted within five years, in which case findings would be renewable for a maximum of an additional three years.

In cases where a company whose exports are the subject of a countervail investigation benefits from subsidy programmes to a much greater extent than other companies exporting the same goods, it may be inequitable to calculate a "residual" margin of subsidization for application to new exporters at the rate of the more heavily subsidized company. To the extent feasible, therefore, in cases where companies exporting the goods that are the subject of a countervail investigation receive widely different degrees of subsidization, company-specific findings could be required for any new exporters of the subject goods.

Current rules provide for the use of undertakings as a method of dealing with injurious subsidized imports before the imposition of countervailing duties. It is important to ensure, however, that these

provisions do not allow selective trade actions to be taken against non-injurious or unsubsidized imports. The provisions governing undertakings could be strengthened by:

- expanding notification requirements to include details of the undertaking itself;
- subjecting undertakings to review and to a sunset clause; and
- clarifying that, in the event that one of the parties to an undertaking requests that an injury investigation be continued and a finding of injury results, the undertaking shall continue in force.

The investigating authorities should also provide, for a reasonable period of time of at least thirty days duration following initiation of any investigation, an opportunity for exporters and importers to respond to allegations by the petitioner and otherwise to provide relevant information. The investigating authorities should also ensure that such responses and information are taken fully into account, such that a preliminary determination of subsidization should not normally be made sooner than sixty days following initiation, unless the product involved has previously been investigated.

The imposition of countervailing duties can have effects that spread well beyond the domestic producers of the like products. Burdens can be imposed on related industries, on consumers and on the domestic economy as a whole. Accordingly, it would be appropriate for countries to provide procedures for formal consideration of whether the imposition of countervailing duties is in the public interest.

Section 3: Non-actionable, non-countervailable subsidies

Current rules do not provide sufficient guidance nor an adequate means of resolving conflicts over which practices are non-distorting. The specification of a category of non-actionable subsidies would contribute greater certainty and predictability to international trade relations.

(a) Conditions for non-countervailability/non-actionability

The most basic condition under which subsidies should be free of any threat of action is general availability. Programmes that are available to the general population, for example for social assistance, public welfare, education, environmental management and conservation, national identity and natural disaster relief, do not distort trade. The concept of general availability could be operationalized by a requirement that no programme that provides grants, forgiveness of debts, loans, loan guarantees or loan insurance, privileged tax treatment or other benefits with equivalent

effect should be countervailed if its benefits are, according to eligibility criteria set out explicitly in laws or regulations, generally obtainable by all industries engaged in:

- (a) manufacturing; or
- (b) primary agriculture; or
- (c) resource extracting/harvesting, including primary processing.

Moreover, the following categories of programmes should be deemed not to be countervailable or actionable:

- regional development assistance generally available to enterprises or industries within designated geographic areas, determined on the basis of neutral and objective criteria using verifiable statistical data;
- assistance to furnish or support basic infrastructure for general public use;
- adjustment assistance provided to workers; and
- assistance to research and development.

(b) Special safeguard procedure - non-actionable subsidies

Situations may arise in which a signatory feels it has been adversely affected by the use of a non-actionable subsidy by another signatory. The need for a special safeguard provision to deal with such situations will depend on the nature of the rules agreed to in the area of non-actionable subsidies.

If a country were of the view that a non-actionable subsidy has been included in the preliminary determination of subsidization, it could refer the matter to a multilateral panel. The panel would be required to issue a report on whether the subsidy in question falls within the non-actionable category prior to the final determination of subsidization by the investigating authority. In the event of an affirmative report by the panel, the importing country would be required to exclude that subsidy from its final determination.

A procedure should also be available to signatories to determine whether a particular practice meets the conditions for non-countervailability/non-actionability. A multilateral panel process would be convened at the request of a signatory. Countries considering the introduction of particular programmes should be able to make ex ante references to that multilateral panel for an advisory opinion on whether a proposed programme would be considered a non-actionable subsidy before the programme is finalized and implemented.

Section 4: Special and differential treatment for developing countries

The Punta del Este Declaration recognizes that the participation of the developing countries in these negotiations is based on consistency with their individual development, financial and trade needs. The procedures and clarifications to current rules suggested within this submission contain elements of particular interest to developing countries:

- greater clarity and precision as to which subsidies are prohibited, actionable or non-actionable;
- improved multilateral procedures, including ex ante rulings, regarding the actionability of particular subsidy practices;
- the establishment of an agreed de minimis level of subsidization below which countervailing duties would not be imposed;
- provision for excluding countries whose exports do not contribute to injury from cumulative injury findings;
- greater certainty in the application of countervailing duties through improved definitions of key concepts such as injury and standards for the identification and calculation of subsidies for the purpose of countervail investigations.

The need for particular provisions with regard to developing countries will depend on the nature of the rules and disciplines which have yet to be developed. We would be prepared to examine proposals that participants wish to present.

Section 5: Notifications and surveillance

Transparency through notifications and surveillance is a key requirement for effective multilateral disciplines on subsidies and countervailing duties. The proposals here for clarification and increased precision as to which subsidy practices are prohibited, actionable and non-actionable would reduce uncertainty regarding what practices are required to be notified. This should reinforce current obligations with respect to notification of subsidies.

As to the need to improve current provisions relating to notification and surveillance, the nature of those improvements will not become clear until there is a clearer sense of what substantive rules are agreed to by the participants. We would also be prepared to examine any proposals in this area.

Section 6: Dispute settlement

Experience with the dispute settlement provisions in the Code has demonstrated that a large number of disputes have not proven susceptible to resolution through the existing process. This is due in large part to the absence of clarity in the obligations and rights associated with the

existing rules. Revisions along the lines suggested within this submission should significantly improve the rules and consequently lead to a more effective dispute settlement process.

Several particular provisions regarding dispute settlement have been suggested in this submission under the various headings of the negotiating framework:

- it would be clear that a violation of the "List of Prohibited Subsidy Practices" would constitute a prima facie case of nullification and impairment;
- procedures would be available for signatories to request rulings on whether other signatories were using prohibited practices;
- a procedure would be established for countries to make ex ante references to multilateral panels for rulings on whether subsidy programmes they propose to implement are prohibited, actionable or non-actionable;
- a special nullification and impairment mechanism would be created whereby any actionable subsidy in excess of a certain maximum level of subsidization would constitute a prima facie case of nullification and impairment;
- a special safeguard procedure would be established to provide recourse to a multilateral panel for a ruling on whether a subsidy that has been included in a countervail investigation is a non-actionable subsidy.

The problems with dispute settlement under the Code, as with dispute settlement generally in the GATT, have manifested themselves in terms of the adoption and implementation of panel reports. Both this Group and the Negotiating Group on Dispute Settlement should address possible improvements to these elements of the dispute settlement process and the relationship of the special multilateral procedures suggested in this submission to the regular dispute settlement mechanism.