

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

RESTRICTED

MTN.GNG/NG10/13

16 October 1989

Special Distribution

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

MEETING OF 26-27 SEPTEMBER 1989

Note by the Secretariat

1. The Group met on 26-27 September 1989 under the Chairmanship of Mr. Michael D. Cartland (Hong Kong). The Group adopted the following agenda:

- A. Discussion of specific proposals on various issues in the framework for the negotiations.
 - B. Arrangements for the next meeting of the Group.
- A. Discussion of specific proposals on various issues in the framework for the negotiations
2. The Group had before it three proposals relating to the framework:
- (a) the comprehensive proposal by Canada (MTN.GNG/NG10/W/25) introduced and preliminarily discussed at the previous meeting;
 - (b) communication from Switzerland (MTN.GNG/NG10/W/26) concerning criteria of allocation of subsidies to the three categories and possible remedies;
 - (c) communication from Japan (distributed at the meeting and subsequently circulated in MTN.GNG/NG10/W/27) covering several elements of the framework.

The representatives of Switzerland and Japan introduced their delegations' proposals.

3. At the Chairman's suggestion the Group agreed on an issue-oriented approach, i.e. that it would discuss selected issues on the basis of relevant specific proposals made under the framework, it being understood that any such discussion would be ad referendum only and that it would not commit any delegation until it knew the outcome of discussion of other issues from the framework. The selection of issues for discussion would depend on actual specific proposals available in time for the meeting. As

the Group had received, in time for this meeting, a proposal dealing with the criteria of allocation of subsidies to the three categories and with possible remedies, the Chairman proposed that the Group concentrate on these two issues on the basis of the three proposals referred to in paragraph 2 above.

Classification of subsidies - prohibited subsidies

4. A number of participants concurred with the view expressed in the Swiss and the Canadian proposals that export subsidies should be prohibited.¹ Some delegations considered that the 1979 Illustrative List should, after some amendments, be made definitive, as this would enhance transparency and predictability. These delegations agreed that such a definitive list could be, from time to time, amended or extended as a result of negotiations in a body supervising the operation of the new agreement. Some other delegation did not see any rationale for converting the illustrative list into a definitive one. They considered that such an approach would open a possibility for circumvention and that any amendments to the list would be practically impossible outside the scope of multilateral negotiations. Some comments were also made on suggestions concerning possible amendments to paragraphs (d), (h), (i) and (j). In particular, some participants supported the proposal that the rules on indirect taxes and remission or drawbacks in paragraphs (h) and (i) should apply to all inputs, and not only to those physically incorporated. Some other delegations considered that such an extension would result in lesser disciplines than the existing ones. Regarding paragraph (d) several participants considered that it did not necessitate any changes.

5. Several participants pointed out that they could not agree to the concept of prohibition unless the present provisions of Article 14 of the Subsidies Code were maintained. They would therefore define their position in the light of the outcome of the discussion on special treatment for developing countries.

6. Some participants expressed their reservation on the proposed category of other trade-related subsidies. They considered that subsidies proposed for this category were already covered by Article III of the General Agreement (subsidies that were contingent upon the use of domestic over imported goods) or by Article XVI:4 (subsidies contingent upon export performance). Some other participants explained that although these subsidies were already prohibited by other provisions of the General Agreement, their inclusion into the category of prohibited subsidies would serve the purpose of better clarity and certainty.

¹Some participants considered that this prohibition should also include export subsidies currently discussed in the Group Agriculture, while others supported the view presented in the Swiss submission that the negotiations on agricultural subsidies should take place in that Group.

7. Several participants expressed strong reservation about the proposed extension of prohibition to some domestic subsidies. It was pointed out that domestic subsidies were often used as an important instrument for the promotion of social and economic policy objectives, and restricting governments' rights to use such subsidies would amount to interference into their sovereignty. It was also recalled that domestic subsidies were generally recognized in economic theory to be a more appropriate instrument of protection than tariffs and therefore there was no economic justification to prohibit them when nobody had ever proposed in the GATT to prohibit tariffs. Another view was that any domestic subsidy could not, per se, be presumed to be trade-distorting, and any judgement could only be made on a case-by-case basis. Those participants therefore wished to make it clear that their participation in the discussion of the proposed criteria should not be construed as their acceptance of the concept of prohibiting certain domestic subsidies. Some other participants reiterated their view that prohibiting some domestic subsidies, i.e. those having a strong direct and negative trade effect, was essential for any improvement of disciplines in the subsidy area.

8. The Group discussed two proposed approaches. The approach presented in MTN.GNG/NG10/W/25 suggested increased disciplines on domestic subsidies in terms of overall subsidization. This concept could be applied on the basis of sector/industry, product or producer/firm and could be defined in terms of "overall" subsidization in excess of X per cent of the value of production. It could also be applied in a manner which simply prohibited grants, loans or equity infusions which exceeded X per cent of the capital cost of a plant, or above a specified absolute level to a firm or industry. Under this approach account, would be taken of assistance offered at various levels of government. Thus, assistance being channelled through sub-national governments, in order to avoid being factored in to the overall subsidization calculation, would not escape disciplines. The approach presented in MTN.GNG/NG10/W/26 relied upon two variables: the subsidy rate (i.e. the amount of subsidy related to the value of the subsidized product) and the import rate (i.e. quantity of the subsidized product exported as compared to the total consumption of the like product in the importing country). Depending on changes in the subsidy rate and the import rate, the subsidy would move from the non-actionable category to the actionable category and even to the prohibited category.

9. Several participants had serious doubts about the rationality of quantitative criteria as they did not see any automatic causal link between the quantum of a subsidy and possible distortive effects on trade. It was pointed out that under the variables' approach there was too much unpredictability as to the nature of a subsidy which could, for reasons totally beyond the control of the subsidizing government, move to the prohibited category. On the other hand some concern was expressed as to various possibilities of circumvention. For example a subsidy having the same displacing effect would be prohibited if the subsidized product was sold in one market but would become non-prohibited or even non-actionable if the sales were dispersed to several markets. It was further pointed

out that the levels of the parameters delineating each category would be very difficult to establish, and given the number of products involved and differing market situations in various countries, they would have to be more or less arbitrary. Some participants, while recognizing technical difficulties, considered that the proposed approaches deserved further exploration and constituted a good basis for further conceptual work.

Classification of subsidies - non-actionable subsidies

10. Some participants said that they attached great importance to this area and stressed the need of a clear understanding of what non-actionable subsidies would be to avoid uncertainty and possible harassment. Some participants considered that exclusion of this class from subsidy disciplines should be subjected to carefully defined conditions, in particular to avoid circumvention of these disciplines. Most participants agreed that, on a normative basis, the main criterion for non-actionability should be the general availability concept. In this regard, it was pointed out that there should be no confusion between government interventions which might not be subsidies at all and subsidies which might be non-actionable. Several participants were of the view that subjecting this class to additional quantitative criteria would be justified as a guarantee against possible trade distorting effects. Some other participants, however, considered that the combination of normative and quantitative criteria might result in uncertainty as to what is really actionable and what is not. Furthermore, the classification of a subsidy could change for reasons beyond the control of the subsidizing country. These participants, therefore, considered that normative criteria would be sufficient to identify this class, with a possible addition of the de minimis rule. Some participants had problems with the proposal that in order for a particular subsidization programme to enjoy the benefits of non-actionability, the subsidizing contracting party should have the obligation to notify this programme to the GATT. They considered that failure to comply with a technical requirement of notification should not result in such serious consequences as rendering a non-actionable programme actionable. Some other participants supported the idea of notification as a condition of non-actionability and considered that it would enhance transparency and clarity in this field.

11. A number of comments were made on the proposed list of non-actionable domestic subsidies. Some participants were of the view that certain measures proposed therein could hardly be considered as subsidies (e.g. environmental aid schemes or schemes for the promotion of cultural values). Several participants had serious doubts as to whether structural adjustment schemes should be included into such a list. It was pointed out that it would be very difficult, if not impossible, to assess the proposed conditions for non-actionability such as insufficiency of private sector efforts. Moreover, most of the structural adjustment programmes resulted in improved competitive capacity of an industry instead of its phasing out. It was also pointed out that there was no economic reason why structural adjustment schemes should be more acceptable and have less trade effects

than various start-off schemes. Under the former, the support went to ailing industries and compensated for financial losses while the latter were destined for legitimate development purposes. A similar comment was made regarding regional development schemes, and several participants had queries about assessment of over-capacity in regional industries. Some participants said that the question of research and development schemes required careful examination as some of these schemes had resulted in direct export payments and subsidized the introduction of a product on a market. It was pointed out that an important condition for non-actionability of those programmes should be that the participation therein and access to their results must be equally open to domestic and foreign enterprises.

Classification of subsidies - actionable subsidies

12. Two approaches to the category of actionable subsidies had emerged from the proposals before the Group. One was to put into this category all those subsidies which did not constitute a prohibited or a non-actionable subsidy. The other one was based on a definition of an actionable subsidy, some elements of which had been provided. Some participants preferred the former approach as more workable and comprehensive. Other participants favoured the latter approach. They felt that there was a need to have a clear definition of what was an actionable (countervailable) subsidy. There was also a need to have a high degree of certainty which could not be assured under the first approach where the border line between categories was quite flexible. In particular it was pointed out that as long as it was not possible to have an exhaustive list of prohibited subsidies on the one hand and of non-actionable subsidies on the other, the residual approach could not be applicable.

13. A number of comments were made on possible elements of a definition of an actionable subsidy. Most participants stressed the criterion of specificity as a conditio sine qua non actionability. Another important criterion for these participants was that of the charge on the public account in the sense of a financial contribution by a government (or revenue foregone). A view was expressed that this concept should cover not only direct but also indirect transfers of funds (e.g. transfer from a government through non-governmental agents) in order to prevent any circumvention. Another view was that this concept was not sufficient as there could be a situation where governments would make certain goods or services available on preferential terms; such practices should also be countervailable. Several participants said that the reference to direct or indirect transfers should not allow to countervail so-called input subsidies.

14. Some participants recalled that in determining the actionability of a subsidy, the question of injury or serious prejudice had to play an equally important rôle. In particular, a reference was made to the need to strengthen the condition of causality and to abandon practices of cumulation and cross-cumulation. It was also pointed out that a de minimis situation should always result in the presumption of no injury.

Remedies - prohibited subsidies

15. A number of participants disagreed with the proposal contained in MTN.GNG/NG10/W/26 that whenever a contracting party demonstrated that subsidies falling into the prohibited category were granted to products imported into its domestic market, it would have a right to impose, without the requirement of an injury test, countervailing duties offsetting the subsidy effect. They considered that a country should not have a unilateral right to establish that another country was in violation of its obligations and to impose remedies. They also pointed out that such a procedure would be inconsistent with the provisions of Article VI of the General Agreement. A view was also expressed that if a remedy was to be proportionate to the negative effects, there was a need to determine the existence and scope of these effects, i.e. injury.

16. Some other participants preferred this approach to the approach proposed in MTN.GNG/NG10/W/25 according to which the appropriate remedy for any violation of prohibition should be recourse to improved dispute settlement procedures and multilaterally sanctioned remedies. They said that under the latter approach the prohibition did not mean much more than some procedural requirements. In their view, however, the purpose of establishing a prohibited category was to identify subsidies which would not be used; at any rate, the violation should not give any right to the violator. They also pointed out that the proposal in W/26 provided a mechanism for prior consultations and multilateral surveillance. These participants considered that the remedy in question should not be confused with a normal countervailing duty action, where the injured party was an industry in a specific country. Here the question was that of a violation of international obligations. If it was established that such a violation had taken place, the incriminated practice would have to be eliminated and the multilateral body should ensure that this happened promptly.

17. Some participants considered that both approaches had elements which would make actions against prohibited subsidies more complicated and subject to longer delays than actions against not prohibited but actionable subsidies, in particular countervailing measures. It was also pointed out that the approach in W/26 did not ensure adequate remedies for a third country market situation. Some other participants expressed the view that the scope and nature of a remedy system should depend on the final scope of prohibitions.

18. A view was expressed that a solution which would ensure elimination or limitation of the incriminated measures was preferable to the application of remedies, in particular in the form of countervailing duties without the injury test. Furthermore, while improvements in the dispute settlement and remedy mechanism might be useful, this should not lead to the multiplication of disputes and their use as a replacement for negotiations.

Remedies - non-actionable subsidies

19. Many participants considered that no action should be possible against non-actionable subsidies and that governments could rely on the fact that they would not be harassed. In this context they reverted to the question of notification as a condition for non-actionability and reiterated their view that the mere fact that a government had not notified a given measure should not have such an important consequence as a denial of non-actionability. They also had some reservations about the rôle of a proposed standing body or panel. A view was expressed that decisions of such a panel on the nature of a governmental intervention might encroach on sovereign rights of governments.

20. Other participants supported the approach in MTN.GNG/NG10/W/26, in particular the quantitative limits on non-actionability which, if exceeded, would result in an assertion that harm had been done and would trigger a multilateral review. They also agreed that failure to notify a subsidy would make it actionable, although this would not mean that action would be actually taken.

Other business

21. The representative of the United States referred to recent initiatives of his Government regarding subsidies in two industrial sectors, namely steel and shipbuilding. He said that circumstances had compelled his authorities to move on subsidies issues in those areas in advance of the conclusion of the work of the Negotiating Group. However, in his view, these initiatives were consistent with the objectives of this Group and the overall Uruguay Round objectives. The centrepiece of these initiatives was to secure agreement on an international consensus designed to introduce greater disciplines, and eventually prohibit certain trade distorting subsidies. They had been fashioned in a manner fully compatible with the subsidies framework set out by Ministers at the Mid-Term Review. Circumstances certainly influenced the timing of these initiatives but incorporation of their results into the conclusion of this Negotiating Group was something which, at this stage, his authorities had every expectation would be accomplished.

22. One participant said that by way of preliminary comment he wished to express his strong expectation that the United States would give priority to the negotiations in this Group and would avoid any action that might jeopardise or further delay these negotiations.

Arrangements for the next meeting of the Group

23. As agreed at the meeting of 27 April 1989, the next meeting of the Group will be held on 19-20 October 1989. At that meeting the Group will continue its discussion of issues in specific drafting proposals from participants. In particular, the Group will revert to issues which were on the agenda for this meeting but, because of time constraints, were not discussed, i.e. remedies against actionable subsidies and special treatment of developing countries.