

**MULTILATERAL TRADE  
NEGOTIATIONS  
THE URUGUAY ROUND**

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Group of Negotiations on Goods (GATT)

Negotiating Group on Subsidies  
and Countervailing Measures

MEETING OF 27-28 MARCH 1990

Note by the Secretariat

1. The Group met on 27-28 March 1990 under the Chairmanship of Mr. Michael D. Cartland (Hong Kong). The Group adopted the following agenda:

- A. Framework for the negotiations - discussion of issues proposed by participants
  - (i) Prohibited subsidies - United States
  - (ii) Net subsidy concept - Canada
  - (iii) Non-actionable subsidies - Japan
  - (iv) Treatment of developing countries - EEC
- B. Arrangements for the next meeting of the Group.

Prohibited subsidies

One participant explained his position that the use of the so-called quantitative approach, i.e. prohibition of subsidies exceeding a specified percentage of total sales and of subsidies granted to firms exporting more than X per cent of their production provided a single, predictable and transparent mechanism. In his view only two pieces of information would be required for the effective operation of this mechanism, i.e. the value of total sales (and export sales) and the amount of subsidies. This information was, normally, publicly available. As the information on total sales was usually available for the preceding year, the calculation of the prohibitive threshold could be made by comparing the preceding year's sales with the current year's subsidies. The question whether the test would be applied to products, companies or industries should be decided on a case-by-case basis. Some allocation problems might arise in the context of multiproduct companies but similar problems had always confronted investigating authorities and could be resolved in the future, as they had been resolved in the past, through a reasonable judgement.

2. Some participants agreed that the existing disciplines on subsidies proved inefficient and that expanding the scope of prohibitions seemed, so far, the only effective way to improve them. They endorsed the need for precision and clarity in this area and recognized that setting certain benchmarks or thresholds might be arbitrary but, at the same time, necessary as the best way to ensure effective disciplines. It was pointed out that disciplines to be worked out had to be enforceable in practice; therefore, further discussion and detailed examination of various approaches was needed. It was also suggested that the quantitative approach could be seen as starting from the same premise as the effect-oriented approach, in the sense that if a large subsidy was granted to a firm and if the firm's output depended on this subsidy, it was obvious that the subsidy in question had an important trade effect. There were, therefore, good reasons to assume, a priori, a significant trade effect of a large subsidy.

3. Some other participants, while recognizing the need for strengthening the subsidy disciplines, considered that this could be done through other approaches than direct prohibitions. This latter approach was too brutal and disregarded varying circumstances under which subsidies might have to be granted. Furthermore, one had to consider important implications of the choice of a quantitative threshold. If it was too high it would encourage subsidization up to that level, if it was too low it would not be accepted by a large number of participants, and therefore many participants would remain outside the scope of subsidy disciplines. It was also pointed out that production and sales of a company or industry varied from one year to another with the consequence that the same subsidy might be permitted in one year and prohibited the following year. This would create instability of economic programmes and lack of certainty for the business community. Several participants found the proposal to prohibit subsidies granted to predominantly exporting firms unacceptable. They considered it biased against countries with small internal markets, where firms were forced to export most of their production to be economically viable. They also considered that the same disciplines should apply to all firms irrespective of whether their sales happened to take place in the domestic or a foreign market.

4. Several participants reiterated their position that domestic subsidies were widely used as important instruments for promotion of social and economic policy objectives and therefore it would not be appropriate to extend the concept of prohibition to any category of domestic subsidies. Furthermore, these subsidies were not aimed at distorting trade and therefore to prohibit them on the assumption that they might have some trade effects was not based on any sound economic rationale. It was also pointed out that developing countries faced a multitude of distortions which needed to be corrected for purposes of their economic development. For that reason also some export subsidies should be excluded from the prohibited category.

5. Some participants said that recently a number of countries had eliminated subsidies because they realized their inefficiency and their distortive effects. The recognition of this seemed to be stronger in the

outside world than in this Group, and therefore if the Group did not build upon the recent tendencies, it might be left behind the real world. The quantitative approach was perhaps brutal and simplistic but it was clear and left little room for ambiguities. Those delegations which favoured a gentler approach should come forward with appropriate proposals. If these proposals could ensure a comparable level of disciplines to the quantitative approach, they would certainly be worth considering.

#### Net subsidy concept

6. One participant explained the rationale behind the net subsidy concept, i.e. the netting out of the amount of domestic subsidies from the total foreign subsidies determined to exist in a countervail investigation. First, there was the fairness or equity rationale, i.e. that the petitioner should come forward with "clean hands". Second, there was the trade distortion or efficiency rationale, i.e. trade might be distorted only if foreign and domestic subsidies had a different impact. While some delegations had argued in this Group that the effects of domestic subsidies were implicitly dealt with through the injury test, in his delegation's view, there was a fundamental asymmetry in the countervail process. The net subsidy concept directly addressed this problem. Several approaches were possible to make it operational. One approach would require that domestic subsidies be treated identically to foreign subsidies throughout the process of investigation of the amount of a subsidy. This would entail simultaneous procedures - a double-tracking of the process - from the complaint stage through to the final determination. The respective per unit levels of domestic and foreign subsidization would be determined and a finding of net subsidy, equal to the foreign subsidy less the domestic subsidy, would be issued. This would add an element of fairness to the countervail process that was currently missing, in that subsidized domestic producers would no longer be able to launch cases against subsidized imports secure in the knowledge that their own subsidies would not be brought to light. Another approach would require the consideration of domestic subsidies at the beginning and at the end of a countervail investigation, but would not entail the double-tracking of the entire process. This approach could mitigate some of the concerns expressed by delegations regarding the administrative burden that might result from the introduction of the net subsidy concept. Once the countervail investigation had proceeded to the stage at which, under current rules, a definitive duty would be imposed, a new rule would make any duties imposed at that point conditional upon the conclusion of a subsequent inquiry into the matter of the net subsidy. This inquiry would constitute a new stage of the countervail process to be conducted after the imposition of "conditional" duties. The investigating authorities would be directed to take account of the information on domestic subsidies received by the complainant companies at this stage. The principal object of the inquiry would be to determine whether, by reason of the receipt of domestic subsidies, a definitive countervailing duty should be assessed in the amount of the net subsidy only, i.e. equal to the full amount of the conditional duty less the level of domestic subsidies received by the complainant. These two approaches should not be considered as definitive of his delegation's views, nor should they be viewed as mutually exclusive.

7. Several delegations supported the "net subsidy concept" and reiterated their views that this concept would ensure more equitable disciplines and might discourage industries from bringing frivolous cases. They expressed their willingness to study in detail some technical and administrative problems involved. Some other participants expressed their serious reservations about this concept. A view was expressed that this concept was inconsistent with the approach reflected in Article 6:3 of the Subsidies Code which provided that injury might be found if "there has been an increased burden on government support programmes". Furthermore, the objective of countervailing duty action was to offset injury caused by subsidized imports and not to deal with subsidies in general. Another view was that this approach was already present in the determination of material injury, where conditions of a domestic industry would reflect the fact that it had been receiving a subsidy. To add the net subsidy concept would result in a double counting. It was also pointed out that subsidies received by a domestic industry were only one element of comparable protection measures and it was unclear why subsidies were included while, for instance, tariffs were not. Some delegations were concerned that the "net subsidy" concept would result in freezing the existing levels of subsidies rather than encouraging their elimination. They also referred to a number of complications (such as lack of a precise definition of a subsidy, treatment of non-actionable subsidies, differences in the calculation of the amount of a subsidy, lengthening of the investigation period, etc.).

#### Non-actionable subsidies

8. One participant said that in his government's view two types of subsidies, i.e. generally available subsidies and specific subsidies with significant social or economic policy objectives, should be clearly defined as non-actionable subsidies. Generally available subsidies did not change the comparative advantage of industries and therefore did not have any trade effects. Specific subsidies with significant social or economic policy objectives were those concerning: (i) structural adjustment, (ii) research and development and (iii) regional development. As to the first group, subsidies which would assist "soft landing" of an industry on the way to closing down or scaling down were necessary to reduce social costs of adjustment caused by, for example, low mobility of labour forces. They should, therefore, be non-actionable within specified time-limits and their short-term effects should be tolerated. As to the second group, a large scale research and development project normally would require a long maturity term, enormous costs and assumption of high technological risks. For these reasons it would often be difficult for private sectors to undertake such projects by themselves. The governments had, therefore, good reasons to help, and if foreign enterprises could participate in the subsidized project and have access to its results on equal terms with domestic enterprises, subsidies to such a project should be classified as non-actionable. Regarding regional development subsidies, if their amount was within the limit necessary to offset the disadvantage of operating in a less-developed region, such subsidies should be classified as non-actionable, because they only promoted relocation of industries in a country.

9. Some participants stressed the significance they attached to the category of non-actionable subsidies. At the same time they pointed out that this category should not be a loophole for avoiding subsidy disciplines and agreed on the necessity to work out clear and stringent criteria for non-actionability. It was pointed out that in the field of structural adjustment, not only subsidies used for "soft-landing" operations but also, under some conditions, subsidies to encourage new investments should be non-actionable. Some other participants said that only subsidies without trade effects or likelihood thereof fell into the non-actionable category. To add anything with actual or potential trade effects would be a major concession. So far no sufficiently stringent criteria had been proposed and there was a risk that subsidies proposed for this category would provide a cover for substantial subsidy policies. This was quite evident regarding environmental policies or policies aimed at security and diversification of energy supply. The latter could simply protect inefficient and high cost energy producers. It was also unclear whether the non-actionability of a subsidy would be judged on its own merits or in conjunction with other programmes. These participants agreed that very strict criteria would have to be worked out before one could decide on the scope of non-actionability.

#### Treatment of developing countries

10. One participant said that the integration of developing countries into the subsidies/countervail disciplines should reflect their economic development and competitive needs. The least developed countries should benefit from the special treatment as provided in Article 14 of the Subsidies Code. Moreover, in the area of countervailing measures, they should be granted larger de minimis market shares which, in many cases, would exclude them from injury determination and, if a measure had to be taken, it should be rather in the form of an undertaking and not countervailing duties. On the other hand, countries which had already achieved a high level of economic development and industrialization, should assume all the obligations of a new Code. The integration into the Code's disciplines of the countries which were between these two groups could be adapted to their competitiveness in given sectors. The criteria which would determine the composition of each group should be clear, precise and automatic. They would be based on global economic indicators in the case of the two first groups and on macro and micro-economic factors for the third group. The basic principle should be that those countries which could afford it, either globally or by sectors, should accept all relevant obligations and this principle should be clearly reflected in the provisions of a new Code. The interpretation proposed at the February meeting of the Group to the effect that Article 14 of the Code provided for appropriate disciplines because it contained a number of provisions to ensure that developing countries did not adopt measures inconsistent with their development needs was not acceptable and the provisions in question not sufficient. He concluded by saying that developing country participants had made their requests known and now it would be important to hear how they expected to participate more fully in the framework of rights and obligations, as provided for in the Punta del Este Declaration.

11. Several participants welcomed this statement and said that special treatment for all developing countries could not go on indefinitely. Indeed, it had become politically and economically impossible to give special treatment to some countries which were highly industrialized and more competitive than many of the OECD countries. A view was expressed that, in accordance with the Punta del Este Declaration, disciplines should take account of individual development needs of developing countries and that special treatment could not be maintained as a permanent regime. New rules should include a dynamic factor and any exception to these rules should not be permanent but phased out within an adequate period. Some participants said that although they could associate themselves with a number of assumptions underlying the statement that had introduced this agenda item, they wished to reflect further on some aspects of this approach. In their view the same disciplines should apply to all, and if a country believed that a specific aspect of these disciplines could not be immediately accepted by it, its situation would be examined with a view to deciding that a transitional period might be necessary. It was also pointed out that general strengthening of the disciplines on subsidies should serve best the interest of small countries with small budgets because such countries could hardly engage in any competitive subsidization. In addition, a number of objectives referred to by developing countries as important for their social and economic needs were or could be met through the use of generally available subsidies falling into the non-actionable category.

12. Several developing participants disagreed with these approaches. Some participants said that the proposal to categorize developing countries into three groups was a political issue with implications going well beyond this Group; it should therefore be discussed in an appropriate forum. Some other participants said that any attempt to create new categories of developing countries would be contrary to the Punta del Este and Montreal Declarations. They recalled that subsidies were an integral part of economic development programmes, necessary to promote social and economic policy objectives. This fact had been recognized in the Subsidies Code and the situation of developing countries had not changed since that time. Article 14 of this Code had a sound economic basis as it recognized the multitude of distortions faced by developing countries, and therefore it should be retained. Developing countries should not be bound by any prohibition of subsidies, in particular as there had been no evidence that developing countries' subsidies had provoked any major economic problems for other participants. On the contrary, it had to be recognized that at the roots of these problems was not the special treatment, but various loopholes in the Code's disciplines which some developed countries were able to use to avoid these disciplines. It was, therefore, suggested that the discussion on the maintenance of the special treatment should not be conducted in abstract or political terms, but it should address specific problems if developed country participants indeed had such problems.

Arrangements for the next meeting of the Group

13. As agreed at the meeting of 20-21 February 1990, the next meeting of the Group will be held on 30 April-1 May 1990. The Group will continue to have on its agenda the discussion of issues in the Framework in order to give an appropriate opportunity for delegations which wish to explore certain issues to do so. In this relation it has been indicated to the Chairman that a number of delegations may wish to raise various issues in the countervailing measures area. The delegations should therefore reflect if they have issues to propose for discussion and, if so, they should inform the Chairman or the secretariat not later than two weeks before the date of the meeting.