Detailed Presentation of Subsidies and Countervailing Measures in the WTO

OBJECTIVES

- Describe the basic WTO disciplines related to subsidies and countervailing measures;
- Explain the different procedures and investigations connected to subsidies and countervailing duties.

I. INTRODUCTION

The WTO Agreement on Subsidies and Countervailing Measures ("the SCM Agreement") both disciplines the use of subsidies, and regulates the actions countries can take to counter the effects of the subsidies of other countries. Under the SCM Agreement, a Member can use the WTO's dispute settlement procedure to seek the withdrawal of the subsidy or the removal of its adverse effects. Or, the Member can launch its own investigation and ultimately charge an additional import duty ("countervailing duty") in the case of subsidized imports that are found to be causing injury to the domestic industry.

WHY DO COUNTRIES USE SUBSIDIES AND WHY DOES THE WTO HAVE AN INTEREST?

Governments use subsidies for a number of reasons. One is market failure, where the market provides less of certain things than the economically optimal level. For example, a new environmental regulation may require businesses to clean up their sites to reduce the level of pollution (following the "polluter pays" principle). An investor considering purchasing and restarting a defunct plant may find that the cost of the required clean-up (of pollution that was caused by the plant's previous owner) is so high that the investment would not be profitable. A government might, in that circumstance, offer a subsidy to the investor to offset some or all of the clean-up cost, in order to ensure that the investment is made. Another example could be where the market does not provide long-term financing, and the government steps in a lender. Depending on the interest rates and other loan terms, the government-provided financing might or might not be subsidized.

Governments also use subsidies as instruments of economic and social policy. For example, a government may wish to ensure that particular stretches of coastline, or particular border areas, are inhabited. It thus may offer subsidies of various kinds for investment and job creation in those areas. Or a government may seek to even out regional economic disparities by offering subsidies for investment and job creation in disadvantaged regions. Or a government may wish to encourage the adoption of certain technologies, or the use of certain kinds of equipment, and thus may offer subsidies to enterprises that do so.

Under the SCM Agreement, most forms of subsidies are allowed, although subject to rules and disciplines. As will be discussed in detail below, only two kinds of subsidies are outright prohibited.

Why does the WTO regulate the use of subsidies? Because regardless of whether they are intended only to correct market failures or to address policy priorities of the government involved, subsidies can distort international markets. In particular, a subsidy can introduce a structural competitive imbalance into the market for a good which is unrelated to the natural comparative advantages of the different countries producing that good. Where this occurs, an unsubsidized good can find it impossible to compete with the subsidized good (as it in effect is competing with the treasury of the subsidizing country), even where the unsubsidized good has the intrinsic comparative advantage.

II. THE AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

IN BRIEF

The **SCM Agreement** disciplines the use of subsidies by Members and regulates the actions Members can take to counter the effects of other Members' subsidies. The SCM Agreement does not prohibit Members from granting most forms of subsidies. It contains rules to determine which programmes, measures, etc. are subsidies, as well as rules governing the use of and disciplines on subsidies, and disciplines on the use of countervailing measures.

The SCM Agreement thus contains two "tracks". The first is the multilateral track, which sets forth the disciplines on governments' use of subsidies, and provides for WTO dispute settlement to enforce those disciplines. Thus, under the multilateral track, a Member concerned over the use of an allegedly prohibited subsidy by another Member, or over the adverse effects allegedly caused by another Member's non-prohibited subsidy, has the right to raise a challenge under the WTO's dispute settlement system. The second track is the unilateral or national track, which is the use of countervailing measures by an importing Member where subsidized imports are causing injury to the domestic industry in the importing Member. (Countervailing measures are similar in form and in terms of procedural requirements to anti-dumping measures, the main difference being that CV measures apply to subsidized, rather than dumped, imports.)

For a measure, programme, incentive etc. to be a "subsidy" in the sense of the SCM Agreement, it must correspond to the legal definition in that Agreement, namely it must involve a financial contribution by a government or any public body within the territory of a Member, which confers a benefit to the recipient. Furthermore, for a subsidy thus defined to be covered by the SCM Agreement and hence subject to its disciplines, the subsidy also must be "specific". Each of these concepts is examined below.

The SCM Agreement classifies specific subsidies into two groups: prohibited subsidies and actionable subsidies. There are only two kinds of prohibited subsidies: export subsidies and local content (or import substitution) subsidies.

The SCM Agreement applies not only to industrial products, but to agricultural products as well. Thus subsidies disciplines and countervailing measures can be invoked in respect of agricultural products. That said, the Agreement on Agriculture modulates some of the multilateral disciplines of the SCM Agreement in respect of those products.

I.A. LEGAL CONTEXT

IN DETAIL

The rules governing subsidies are contained in the SCM Agreement while the Agreement on Agriculture contains specific rules governing the use of agricultural subsidies.

THE HISTORICAL BACKGROUND TO THE SCM AGREEMENT

Rules on the use of subsidies and countervailing measures have been part of the multilateral trading system since the beginning. In particular, Article XVI of GATT 1947 contained the original rules on subsidies, and Article VI (which also covers anti-dumping) contained the original rules on the use of countervailing measures.

These original rules were, however, relatively general. For instance, Article XVI of GATT 1947 did not define the term "subsidy" and contained little detail as to the types of adverse effects that might be caused by subsidies or as to the actions other Contracting Parties could take in response. Article VI contained only three paragraphs regarding the use of countervailing measures.

In response to the need to elaborate on the GATT rules on subsidies and countervailing measures, the Tokyo Round of multilateral negotiations, which took place between 1973 and 1979, saw the creation of the Agreement on Implementation and Application of Articles VI, XVI and XXIII of the General Agreement, generally known as the "Tokyo Round Subsidies Code", or "Subsidies Code". .

Unfortunately the Subsidies Code, which was a plurilateral agreement, did not fully achieve its purpose. It was ratified by only twenty -five Contracting Parties, and under it there were a number of disputes including over fundamental concepts that were not defined in the Code.

Therefore, in the Uruguay Round, the rules on subsidies and countervailing measures were once again put on the negotiating agenda. The Punta del Este Ministerial Declaration, which launched the Round, called for a fundamental review of all of the rules on subsidies and countervailing measures: Articles VI and XVI of the GATT 1947 and the Subsidies Code. The final result of these negotiations was the SCM Agreement.

THE SCM AGREEMENT

The SCM Agreement builds upon the Subsidies Code and the original GATT provisions. Unlike those predecessors, the SCM Agreement contains a definition of subsidy and introduces the concept of the "specificity" (selective availability) of a subsidy. Only specific subsidies are subject to the disciplines set out in the SCM Agreement.

The object of the SCM Agreement is to impose multilateral disciplines on subsidies that distort international trade. The SCM Agreement also regulates WTO Members' reactions against subsidized imports. Subsidies result from the decisions of governments. The provisions of the SCM Agreement not only regulate the unilateral action (countervailing duties) that may be taken against subsidized imports, but also establish multilateral disciplines to control the use of subsidies themselves.

The SCM Agreement, forming part of the single undertaking under the WTO Agreement, applies to all WTO Members, developed and developing (in contrast to the Subsidies Code which applied only to its signatories). The SCM Agreement contains special provisions in favour of developing countries, which are perhaps the broadest and most significant of those in any WTO agreement.

Furthermore, the SCM Agreement goes far beyond its predecessors in terms of the level of detail and specificity of the rules in respect of subsidies. It establishes detailed disciplines in respect of both prohibited and non-prohibited subsidies, including definitional provisions on prohibited subsidies, lengthy provisions concerning adverse effects of subsidies, and details as to the applicable multilateral dispute settlement procedures. It also expands upon the provisions of the Subsidies Code in respect of the use of countervailing measures

From 1995 – 2003, the so-called "implementation period" under the Agreement on Agriculture, WTO Members' ability to challenge other Members' agricultural subsidies under the SCM Agreement was subject to a number of constraints, so long as the subsidizing Member fully conformed to its commitments under the Agreement on Agriculture. Among these constraints was that domestic agricultural subsidies that had no or at most minimal trade- or production-distorting effects, and that conformed fully to the provisions of Annex 2 (the so-called "green box") of the Agreement on Agriculture, could not be subjected to countervailing duties. There also were limitations on the multilateral challenges that could be brought in respect of agricultural export subsidies and domestic support measures that were fully consistent with the subsidizing Member's commitments under the Agreement on Agriculture. Other than the subsidies covered by the green box, however, agricultural subsidies remained countervailable (although subject to a "due restraint" clause on initiation). This so-called "peace clause" was contained in Article 13 of the Agreement on Agriculture.

With the expiry of the implementation period at the end of 2003, the peace clause also expired. The Agreement on Agriculture nonetheless continues to modulate, in certain cases, the SCM Agreement's disciplines as they apply to agriculture subsidies.

TIP

It is important to note that pursuant to Article 21 of the Agreement on Agriculture, in case of conflict between the Agreement on Agriculture and any agreement in Annex 1A to the WTO Agreement, including the SCM Agreement, the provisions of the Agreement on Agriculture prevail.

I.B. INTRODUCTION

I.B.1. TWO AGREEMENTS IN ONE: THE TWO TRACKS

The Agreement on Subsidies and Countervailing Measures, as its name indicates, addresses two separate but closely related topics: multilateral disciplines regulating the provision of subsidies, and the unilateral or national use of countervailing measures by a Member to offset injury in its territory caused by subsidized imports.

Multilateral subsidies disciplines are the rules governing whether or not a subsidy may be provided by a Member, and regulating the adverse trade effects that a subsidy may cause. These disciplines are enforced through invocation of the WTO dispute settlement mechanism.

Countervailing duties are a unilateral instrument, which may be applied by a Member to imports of a product into its territory, on the basis of an investigation in which the imports in question are found to be subsidized, and to be causing injury to the domestic industry of the importing Member.

The following diagram summarizes the main features of each track:

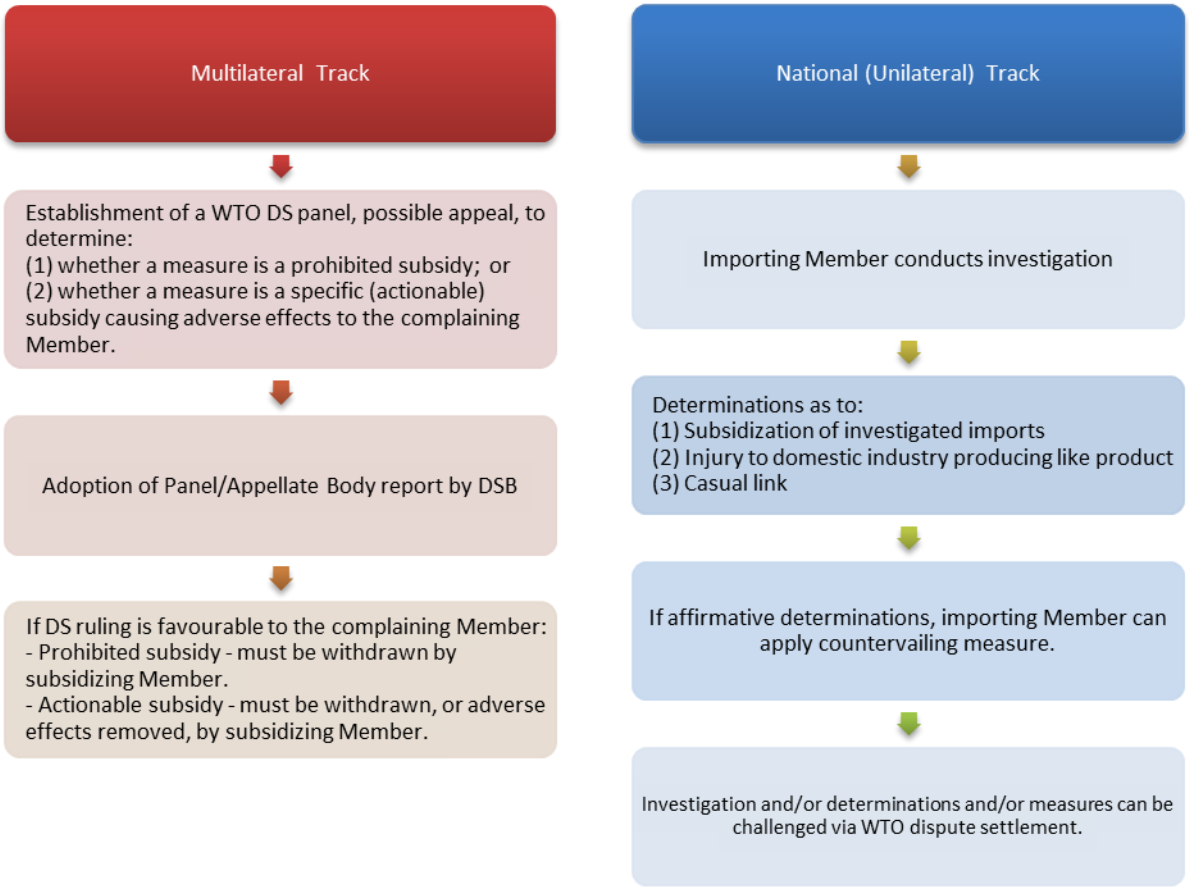


Figure 1: Main features of the two tracks of the SCM Agreement

As we will see in the next section, some parts of the SCM Agreement apply to only one of the tracks, while other parts apply to both. For instance, Part I "General Provisions" defines the measures subject to the Agreement, and thus the measures that must be notified and that can be challenged in dispute settlement or subjected to countervailing measures. Thus Part I is relevant to both tracks. By contrast, Part II contains disciplines on prohibited subsidies, and thus is relevant only to the multilateral track, while Part V contains the rules on countervailing measures and thus is relevant only to the unilateral track.

I.B.2. STRUCTURE OF THE AGREEMENT

The SCM Agreement contains 11 parts:

- Part I contains the fundamental definitional provisions, of "subsidy" and of "specificity", and further provides that only measures constituting specific subsidies in the sense of these definitions are covered by the SCM Agreement.
- Parts II and III divide all specific subsidies into one of two categories: prohibited and actionable, respectively, and establish certain substantive disciplines, as well as dispute settlement rules, with respect to these categories.
- NOTE: Part IV, applicable to non-actionable subsidies, expired at the end of 1999.

- Part V establishes the substantive and procedural requirements for application by a Member of countervailing measures.
- Parts VI and VII establish the institutional structure and notification and surveillance mechanisms for implementation of the SCM Agreement.
- Part VIII contains special and differential treatment rules for various categories of developing Members.
- Part IX contains transition rules for non-developing Members to bring their non-conforming measures that existed as of the entry into force of the SCM Agreement into conformity with it. Separate rules applied to developed Members and Members in transformation to market economies.
- Parts X and XI contain dispute settlement and final provisions.

I.C. COVERAGE OF THE SCM AGREEMENT

Part I of the Agreement defines the coverage of the Agreement. Specifically, it establishes definitions of the terms "subsidy" and "specificity". As noted above, only "specific subsidies" within the meaning of Part I are subject to the SCM Agreement's multilateral disciplines and can be countervailed.

I.C.1. DEFINITION OF SUBSIDY

IN BRIEF

Unlike the Tokyo Round Subsidies Code, the SCM Agreement contains a definition of the term "subsidy". The definition contains three basic elements: (i) a financial contribution (ii) by a government or any public body within the territory of a Member (iii) which confers a benefit. All three of these elements must be present for a subsidy to exist. Remember, however, that not all "subsidies" are covered by the SCM Agreement. Rather, only those that are "specific" are covered.

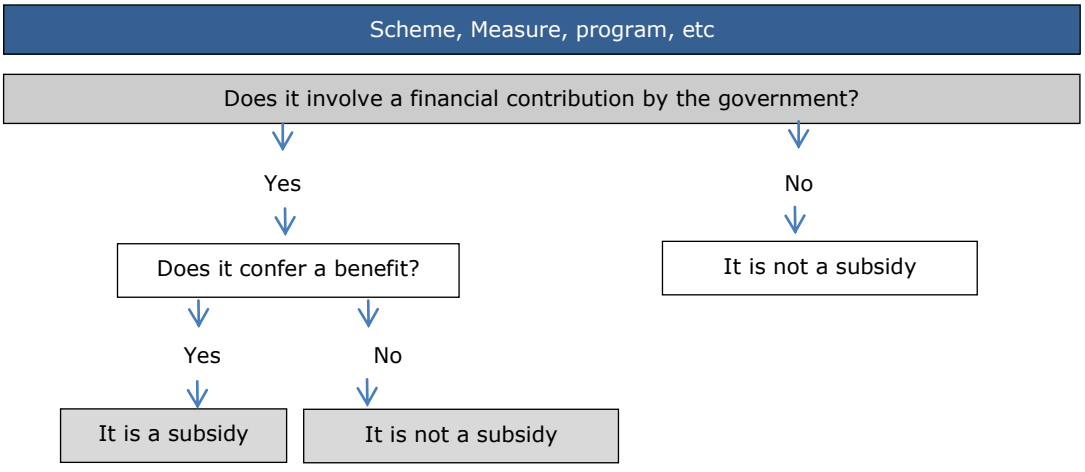


Figure 2: What is a subsidy

IN DETAIL

FINANCIAL CONTRIBUTION

Pursuant to Article 1.1 (a)(1) of the SCM Agreement, only measures in the form of a "financial contribution" may be subsidies. This provision sets forth a closed (exclusive) list of the types of measures that constitute financial contributions, namely:

- Direct transfer of funds (example, a grant, a loan, etc.);
- Potential direct transfer of funds or liabilities (example, a loan guarantee);
- Government revenue otherwise due that is foregone or not collected (example, fiscal incentives such as tax credits);
- Government provision of goods or services other than general infrastructure, or government purchase of goods;
- Government payment into a funding mechanism.

In addition, certain income or price support also is listed as potentially constituting a subsidy, if it confers a benefit.

TIP

The term "financial contribution" as used in the SCM Agreement does not connote, by itself, that there is a subsidy (in the sense of a "gift" from the government). Rather, this term simply connotes the transfer of something of value. Whether there is a subsidy depends on the terms of this transfer, which is where the concept of "benefit", discussed below, comes into play.

BY A GOVERNMENT OR PUBLIC BODY

For a financial contribution to be deemed a subsidy for the purposes of the SCM Agreement, the financial contribution must be made by government or a public body. A government can be at the national or sub-national level, and can be any sort of governmental entity. A public body is an entity other than a government, but which has or fulfils some sort of public policy role. A financial contribution made by a private body may still fall under the definition in Article 1.1 of the SCM Agreement if that contribution was made pursuant to entrustment or direction by the government.

What happens where both parties involved in a transaction, for instance the bank granting a loan and the company receiving it, are private entities? If the government or any public body has entrusted or directed a private body, in this case the bank, to make the loan, the financial contribution is, for purposes of the Agreement, made by the government. If there is no evidence of such entrustment or direction, however, the loan cannot be attributed to the government, and thus will not be covered by the SCM Agreement, meaning that it cannot be subject to WTO dispute settlement or to countervailing measures.

Also, it is not only (the subsidies of) national-level governments and public bodies, but also (those of) all sub-national levels of government and public bodies that are subject to the SCM Agreement. Thus, if a provincial or municipal government provides a subsidy, this is fully subject to the disciplines of the SCM Agreement.

CONFERRING A BENEFIT

Pursuant to the SCM Agreement, a financial contribution by a government does not involve a subsidy unless it confers a "benefit". In many cases, as in the case of a cash grant, the existence of a benefit will be clear. A grant, being a gift, confers a benefit in its full amount, as the recipient does not have to pay anything for it. In some cases, however, the issue of benefit will be more complex. For example, when does a government loan, a government equity infusion, or the provision or purchase by a government of a good confer a benefit?

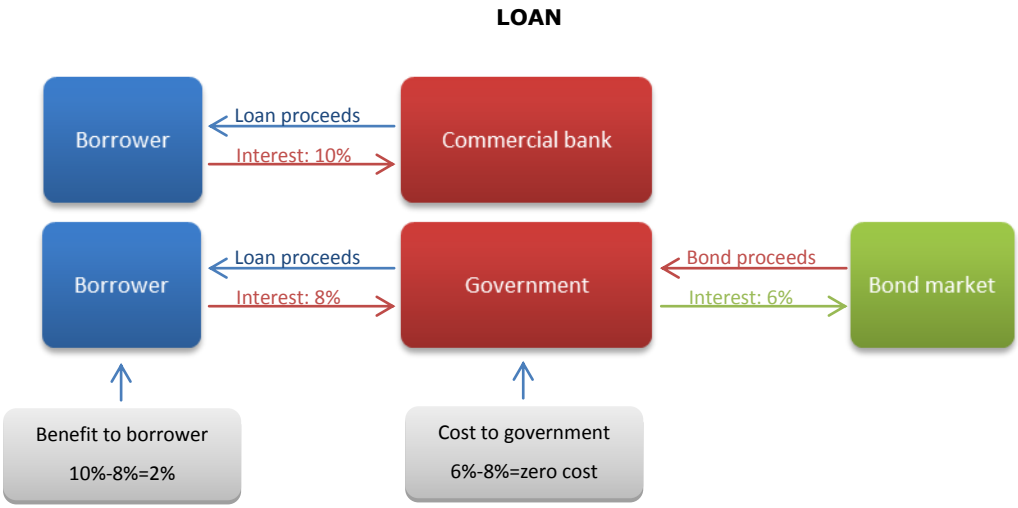
Although the SCM Agreement does not provide complete guidance on these issues, the Appellate Body has ruled that the existence of a benefit is to be determined by comparison with the market-place. The question to be answered is therefore whether the financial contribution is "provided on terms which are more advantageous than those that would have been available to the recipient on the market." If the answer is positive, then the financial contribution confers a benefit. So, for example, a government-provided loan confers a benefit where its terms are more favourable to the recipient than those the recipient could have obtained from a commercial lender. Similarly, government provision of goods confers a benefit where the price charged for the goods by the government is less than the prevailing market price for those goods, in the country where the goods are provided.

The SCM Agreement provides some, albeit not complete guidance on the question of benefit, in the form of guidelines for calculating the amount of subsidy in terms of the benefit to the recipient, for purposes of countervailing duty investigations (addressed in detail below). These guidelines have been found by panels and the Appellate Body also to be useful in determining the existence of a benefit (for purposes of determining whether a measure is or is not a subsidy). The guidelines address how to determine benefit for four different forms of financial contribution: (1) equity infusions by the government - the market-based comparison is with the "usual investment practice of private investors"; (2) government loans - the market-based comparison is with a comparable commercial loan that the borrower could actually obtain on the market; (3) government loan guarantees - the market-based comparison is with what the borrower would pay for the loan on the market in the absence of the guarantee; and (4) government provision of goods or services, or government purchase of goods - the comparison is with the prevailing terms and conditions in the market where the provision or purchase takes place, to determine if the price paid to the government is too low (in the case of government provision of goods or services), or the price paid by the government is too high (in the case of government purchase of goods).

It may seem that if a government incurs a net cost when it makes a financial contribution then the recipient automatically receives a benefit. This is not necessarily the case. Rather, the existence of a benefit is independent of whether or not the government incurs a cost in providing the financial contribution.

The following diagram illustrates this point, using the example of a government loan to company. In the example, although the government actually makes money on the transaction, by lending the money at a higher interest rate than its own cost of funds, the loan recipient nonetheless receives a benefit, as it obtains the government loan for a lower interest rate than it could have obtained from a commercial lender.

No cost to Government but benefit. Example:



By contrast, a government might incur a cost in providing a certain financial contribution, without conferring a benefit. For example, a government might provide inputs to a producer of a particular product. Assuming that the government is a high-cost producer of those inputs, it might have to incur a loss in order to sell them at the prevailing market price, in which case there would be a cost to the government. Assuming that the government simply meets the prevailing market price, however, the company purchasing from the government rather than from a private supplier would not receive a benefit, and thus there would be no subsidy, in spite of the cost incurred by the government.

In analysing a measure under the SCM Agreement, it is important to separate completely the concepts of financial contribution and benefit.

Whether a given measure, programme, incentive, etc. constitutes a financial contribution does not depend on and should not be mixed with whether it confers a benefit. Rather, a measure will constitute a financial contribution only if it takes one of the forms listed in the SCM Agreement. If the measure does not take one of these forms, then even if it confers a measurable benefit to a company or a sector of the economy, it is not a subsidy and thus cannot be subject to the disciplines of the SCM Agreement.

I.C.2. SPECIFICITY

Assuming that a measure is a subsidy within the meaning of the SCM Agreement (i.e., a financial contribution that confers a benefit), it nevertheless is not subject to the provisions of the SCM Agreement unless it is specific to, i.e., provided on a selective basis to, to a particular enterprise or industry or group of enterprises or industries, or to a particular region.

The basic principle is that a subsidy that distorts the allocation of resources within an economy should be subject to discipline. Where a subsidy is widely available within an economy, such a distortion in the allocation of resources is presumed not to occur. Thus, only "specific" subsidies are subject to the SCM Agreement disciplines. Four types of "specificity" are identified in the SCM Agreement:

- Enterprise specificity: Access to a subsidy is limited to a particular company or companies.
- Industry specificity: Access to a subsidy is limited to a particular industry or industries.

- Regional specificity: Access to a subsidy is limited to recipients located in a geographical region within the jurisdiction of the granting authority.
- Prohibited subsidies: These subsidies are automatically deemed by the SCM Agreement to be specific.

The SCM Agreement covers not only subsidies to which access is *explicitly* limited, in the law or by the granting authority, to certain enterprises (so-called *de jure* specificity). It also covers subsidies to which access is limited *in fact* (so-called *de facto* specificity). A subsidy which by law can only be provided to a given company or a given sector, for example, would be specific *de jure*. In many cases, however, there is no such explicit limitation of access to the subsidy in the law, or established by the authority granting subsidy. Specificity can still be established, nonetheless, if the facts demonstrate that in practice the subsidy is limited to only certain of the nominally eligible recipients. The factors that can be considered in assessing whether an apparently non-specific subsidy in fact may be specific are:

- The use of the subsidy by a limited number of certain enterprises.
- The predominant use of the subsidy by certain enterprises,
- The granting of disproportionately large amounts of subsidy to certain enterprises.
- The manner in which discretion has been exercised by the granting authority in making its decisions about granting the subsidy.

The Agreement contains provisions for identifying subsidies that are not specific. In short, specificity cannot be found where eligibility for the subsidy is based on objective criteria, which are set forth explicitly in law, regulation or other official document, so as to be capable of verification, and those criteria are strictly adhered to and are applied in an automatic manner. Objective criteria are defined as criteria that are neutral, that do not favour certain enterprises over others, and that are economic in nature and horizontal in application. Examples given are the number of employees or the size of the enterprise. Thus, an investment tax credit available to any enterprise that invests at least $100,000, or that creates at least 10 new jobs, to which access is automatic so long as these criteria are met, would not be specific. (Specificity could only be found if the criteria were not strictly adhered to, and access was not automatic, and otherwise there was evidence to show that the programme was operated in a *de facto* specific manner.)

In assessing whether or not a subsidy is *de facto* specific, on the basis of the above and any other relevant factors, account must be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority, as well as of the length of time during which the subsidy programme has been in operation. This is to avoid unjustified findings of specificity. For example, if in a given country there are two main industries, the fact that these industries are the main users of the subsidy programme at issue may simply reflect the structure of the economy, rather than targeting of subsidies to them by the government. Similarly, if a subsidy programme has only been in existence a short time, the fact that the range of actual users of the programme is limited compared with the universe of those eligible may simply reflect the fact that other potential users have not yet become aware of the programme, rather than any deliberate targeting by the government.

Finally, subsidies that are contingent on export performance, and subsidies that are contingent on the use of domestic over imported goods (the prohibited subsidies) are defined in the SCM Agreement as being *per se* specific. That is, the existence of the contingency in question, which is what makes the subsidy in question prohibited, automatically satisfies the specificity requirement of the SCM Agreement. Both the contingency on export performance and the contingency on the use of domestic goods can be established on *a de jure* or a *de facto* basis,

The following diagram illustrates how "specificity" works under the SCM Agreement:

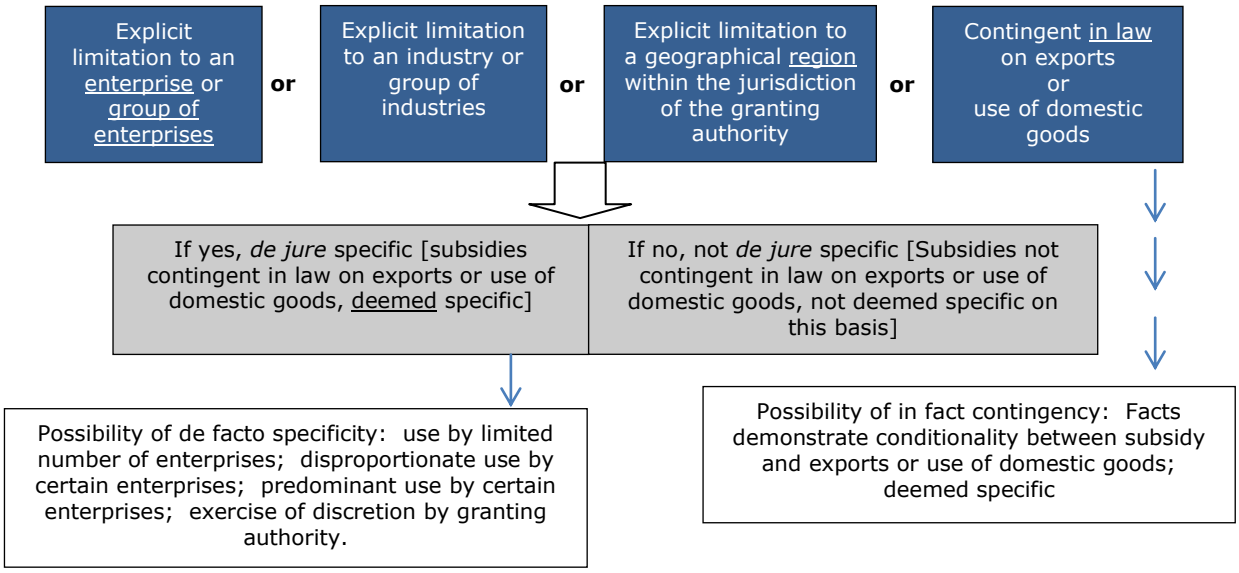


Figure 3: How "specificity" works under the SCM Agreement

I.C.3. ILLUSTRATION 1

Now, let's apply the basic concepts and definitions of subsidy and specificity to an example. The law of Country A establishes a minimum salary of USD500 per week, and further provides that workers cannot work more than 35 hours per week. To improve the competitiveness of the wagon wheel sector, the Government of Country A issues a proclamation pursuant to which the minimum salary and the maximum number of hours worked per week do not apply to that sector. As a consequence, wagon wheel producers in Country A have an advantage in terms of labour costs over companies in other industries and sectors of the economy.

It could certainly be argued that the measure (i.e., the non-application of the legally-required minimum salary and maximum working hours) confers a tangible, measurable benefit to the wagon wheel industry, in the amount of labour costs saved. And it is clear that the measure is a governmental measure, given that it was created via an official proclamation. Furthermore, because the measure is limited to only one sector of the whole economy of Country A, it is specific, and as this limitation is explicitly set forth in the proclamation, the specificity is *de jure*. Do all of these facts mean that the measure is subject to the SCM Agreement? Not necessarily, because in the first place the measure must constitute a financial contribution, as defined by the SCM Agreement, to be potentially covered thereby.

In this regard, a measure such as the one described above – an exemption from legal requirements as to minimum salary and maximum number of working hours per week – does not correspond to any of the types of financial contributions listed in the Agreement. In particular, it is not a transfer of funds (either direct or potential direct); it is not the non-collection of revenue that otherwise would be due to the government; it is not the provision of goods or services, or the purchase of goods, by a government; and it is not the payment by the government into a funding mechanism. Given that the measure does not fit within the definition of a financial contribution, it cannot give rise to a subsidy in the sense of the SCM Agreement, and thus is not subject to the disciplines of that Agreement, in spite of being a *de jure* specific governmental measure that confers a benefit.

Now, let's change the facts, and assume that everything else is the same except for the form of the measure. In particular, let's now assume that the measure is a government grant programme, under which wagon wheel producers can obtain an investment grant of USD 10,000 for every USD 500,000 that they invest in new energy-efficient plant and equipment. Once again, the measure is established via government proclamation, and the proclamation specifies that only wagon wheel producers are eligible. Would this measure be covered by the SCM Agreement? Yes. As in the first scenario, the measure is governmental, and it is *de jure* specific to the wagon wheel industry, based on the proclamation. Being in the form of a grant, it clearly confers a benefit (as grants are gifts). Finally, again because it is in the form of a grant, it clearly falls within the SCM Agreement's list of financial contributions (it is a "direct transfer of funds"). Being covered by the Agreement does not mean that the measure is illegal. Because in our example the subsidy is not contingent on exporting or on the use of domestic goods, it is not a prohibited subsidy; rather it is actionable. This means that if harms the trade interests of another Member in any of the ways specified in the SCM Agreement, that other Member can take action (either under the multilateral subsidies disciplines or by imposing a countervailing measure), if all of the requisite conditions are met.

EXERCISES:

1. Does there have to be a monetary payment for a subsidy to exist?
2. Does the SCM Agreement cover subsidies given at a sub-national level?
3. Would a special three-year exemption from a pollution tax, provided to one industry, be a measure covered by the SCM Agreement?
4. Are subsidies on agricultural products subject to the SCM Agreement?

I.D. CATEGORIES OF SUBSIDIES UNDER THE SCM AGREEMENT

Since 2000, with the expiry of the provisions related to non-actionable subsidies (see Tip below), the SCM Agreement regulates two basic categories of subsidies: those that are prohibited, and those that are actionable (i.e., not prohibited but potentially subject to challenge on the basis of adverse effects, or to countervailing measures). All specific subsidies fall into one of these categories.

TIP

For the first five years after its entry into force, the SCM Agreement contained a third category of subsidies, non-actionable, or "green light" subsidies. (The non-actionable subsidy provisions were contained in Articles 8 and 9 of the SCM Agreement.) The non-actionable subsidies were certain narrowly-defined specific subsidies for research and development, for adaptation of existing facilities to new environmental regulations, and for assistance to disadvantaged regions. These subsidies were selected for non-actionable status on the basis that they furthered important policy goals and were unlikely to have harmful effects on trade. The provisions on non-actionable subsidies applied provisionally for a period of five years, and expired at the end of 1999. The covered subsidies thus reverted to actionable status at that time. Provisions on presumed serious prejudice from certain (other) kinds of subsidies expired at the same time. See Tip below.

The SCM Agreement adopts what is sometimes called a "traffic light" approach in categorizing different types of subsidies:

1. Prohibited. "Red light" or "red" subsidies: Prohibited on the basis of their (irrebutably) presumed adverse effects on trade. There are two types of prohibited subsidies:

- Subsidies contingent, in law or in fact, upon export performance, ("export subsidies").
- Subsidies contingent upon the use of domestic over imported goods("import substitution" or "local content" subsidies).

TIP

Annex I to the SCM Agreement contains an illustrative NON-exhaustive list of eleven types of export subsidies. The listed subsidies are *per se* export subsidies. Measures not listed in the Annex must be analysed to determine whether they meet the definitions of "subsidy" and export contingency.

Prohibited subsidies are subject to special and additional dispute settlement rules (i.e., in addition to those in the Dispute Settlement Understanding). One such special rule is that if a challenged subsidy is found to be prohibited, the remedy is that the subsidy must be withdrawn immediately.

2. Actionable. "Yellow light" or "amber" subsidies: Actionable, i.e., subject to challenge, on the basis of evidence that they have caused specified adverse effects, in particular cases. (That is, there is no presumption of adverse effects in respect of actionable subsidies. But see the Tip below.)

There are three types of adverse effects on the basis of which a Member can bring a dispute against another Member's subsidies:

- **Serious prejudice** - this can take a number of specified forms, including: displacement or impedance of imports of a "like product" into the market of the subsidizing Member; displacement or impedance of exports of a "like product" into a third country market; significant price undercutting, price suppression or depression, or lost sales; in the case of a primary product, an increase over historical levels in the world market share of the subsidized product.
- **Injury** - injury to the domestic industry producing the like product in the importing country, caused by subsidized imports.
- **Nullification or impairment of benefits** - Where the effect of the subsidy in the territory of the subsidizing Member is to prevent trading partners from enjoying the benefits of multilateral market access concessions that they have received from the subsidizing Member.

Members considering that they are subject to serious prejudice, injury or nullification or impairment of benefits can refer the matter to the Dispute Settlement Body. In the area of actionable subsidies, the SCM Agreement contains certain special and additional dispute settlement rules. One such rule is that if a challenged subsidy is found to be causing specified adverse effects, the subsidizing Member must withdraw the subsidy or remove the adverse effects.

TIP

Through the end of 1999, four specified types of actionable subsidies were "deemed" (that is, rebuttably presumed) to cause serious prejudice. (This presumption was contained in Article 6.1 of the SCM Agreement.) The subsidizing Member could rebut such a presumption by demonstrating (on the basis of evidence) that in fact the subsidies at issue did not cause any of the forms of serious prejudice referred to above. The provisions on presumed serious prejudice and on non-actionable subsidies were negotiated as a package during the Uruguay Round. Both sets of provisions were in force for a provisional period of five years (through the end of 1999) and both could have been extended by consensus of the Committee on Subsidies and Countervailing Measures ("SCM Committee"). No such consensus was reached, and all of these provisions thus lapsed simultaneously.

3. Non-actionable, or "green": Lapsed 31 December 1999.

IF YOU WANT TO KNOW MORE...

AFTERMATH ON NON-ACTIONABLE SUBSIDIES

Pursuant to Article 31 of the SCM Agreement, the non-actionable subsidies provisions (as well as the deemed serious prejudice provisions) could have been extended for a further period, beyond 1999, on the basis of a consensus of Members in the SCM Committee. Certain developing Members insisted, in the Committee's review of whether or not to extend these provisions, that non-actionability be refocused or at least broadened to address subsidies of specific interest to developing Members. No consensus on extension of these provisions (with or without modification) was reached by 31 December 1999, the end of the five-year period, and the provisions therefore lapsed. The issue was re-raised by certain developing Members at the Doha Ministerial Conference, where the Doha Round was launched. In this connection, paragraph 10.2 of the Doha Ministerial Decision on Implementation-Related Issues and Concerns referred the question of non-actionability for certain subsidies of developing Members to the relevant negotiating

group (the Negotiating Group on Rules). No specific textual proposals on this issue have been tabled in the negotiations, however.

I.D.1. PROHIBITED SUBSIDIES - EXPORT SUBSIDIES

For a subsidy to be an export subsidy prohibited under the SCM Agreement, it must be "contingent" upon export performance, whether solely or as one of several conditions. This means that eligibility for the subsidy depends in some way, at least to some extent, on the recipient's export activities. In other words, contingency on export performance has to do with the eligibility criteria for obtaining the subsidy, and in particular those criteria must include export activities in some way. Furthermore, the export criterion may either be explicit (de jure) or evident from the facts surrounding the granting of the subsidy (de facto).

An example of a subsidy that would be de jure contingent upon export performance is a grant programme for which the eligibility criteria are that the recipient be located in a particular region, that it be in one of three specified industries, and that at least 4 per cent of its total sales be export sales. Notwithstanding the existence of the other (non-export-related criteria), the fact that one of the criteria is a minimum level of export sales renders this subsidy contingent on export performance. As such, it would be a prohibited subsidy.

Determination of de facto export contingency is considerably more difficult. In particular, it is necessary to look at the facts surrounding the granting of the subsidy to ascertain the extent to which exportation, or anticipation of exportation, figured in the granting authority's decision to provide the subsidy.

CASE STUDY 1

This case study, of an actual dispute, demonstrates inter alia one approach that has been followed in determining de facto export contingency.

CANADA — MEASURES AFFECTING THE EXPORT OF CIVILIAN AIRCRAFT (DS70)

Parties		*Agreements*	*Timeline of the Dispute*	
Complainants	Brazil	SCM Agreement Articles. 1, 3.1 and 4.7	Establishment of Panel	23 July 1998
			Circulation of Panel Report	14 April 1999
Respondent	Canada		Circulation of AB Report	2 August 1999
			Adoption	20 August 1999

1. Measure and Industry at Issue

- Measure at issue: Canadian measures providing various forms of financial support to the domestic civil aircraft industry.
- Industry at issue: Civil aircraft industry.

2. Summary of Key Panel / AB Findings

- ASCM Art. 1.1 (subsidy): The Panel found that a "financial contribution" confers a "benefit" and constitutes a subsidy under Art. 1 when provided on terms more advantageous that those otherwise available to the recipient on the market. The Appellate Body, in upholding this finding, concluded that the word "conferred", in conjunction with "thereby", calls for an inquiry into what was conferred on the recipient, not an inquiry into the cost to the government as argued by Canada.
- ASCM Art. 3.1(a) (export subsidies): The Appellate Body upheld the Panel's finding that contingency upon export performance exists if there is a relationship of conditionality or dependence between the grant of the subsidy and the anticipated exportation or export earnings.
- Examination of Canada's individual measures: The Panel concluded that the evidence did not demonstrate that the "EDC" programme was contingent on export performance. The Panel also found that the "Canada Account" programme was in some cases providing subsidies contingent on export performance. Regarding the "TPC" programme, the Panel also that the "the facts demonstrate[d] that [TPC contributions] would not have been granted but for anticipated exportation". The Appellate Body upheld these findings by the Panel. The Panel and Appellate Body considered that the entire constellation of the facts surrounding the decisions to grant the subsidies at issue demonstrated the export contingency.

The SCM Agreement contains, in its Annex I, an "Illustrative List of Export Subsidies". The Agreement provides that any measure identified in the List as an export subsidy automatically fulfils the definitions of subsidy and contingency on export performance. That is, these measures, *per se*, are export subsidies for purposes of the SCM Agreement. Certain panels have found, however, that it is not permissible to read any item in the List in an inverse sense to determine whether a measure is not an export subsidy. Rather, only where the List explicitly identifies something as not being an export subsidy can that conclusion be drawn.

I.D.2. PROHIBITED SUBSIDIES - IMPORT SUBSTITUTION SUBSIDIES

For a subsidy to be prohibited under the SCM Agreement as an import substitution subsidy, it must be "contingent" on the use of domestic over imported goods. As in the case of export subsidies, the concept of contingency means dependence or conditionality - eligibility for the subsidy must depend or be conditioned on the use of domestic goods. This contingency can be one among several other factors, and it can be either *de jure* or *de facto*. It should be noted that the possibility of establishing this conditionality on a *de facto* basis is not expressly set forth in the SCM Agreement. The Appellate Body nevertheless has found that the provision encompasses *de facto* as well as *de jure* conditionality.

I.D.3. ACTIONABLE SUBSIDIES - GENERAL

Under the actionable subsidies provisions, there are a number of forms of adverse effects caused by subsidies that a complaining Member can allege before a WTO dispute settlement panel. In all cases, the assessment is fact-specific. It is not sufficient (as in the case of prohibited subsidy disputes) to establish that the subsidy in question, as alleged, exists. Rather, for actionable subsidies, not only must it be established that there is a specific subsidy, it also must be demonstrated that the subsidies provided benefit the production, sale, marketing, etc. of the product in question, and that the subsidized competition causes harm to the trade

interests of the complaining Member, in respect of the same product. The causation analysis must include a non-attribution analysis, to ensure that harm caused by other factors is not attributed to the subsidies at issue.

I.D.4. ACTIONABLE SUBSIDIES - SERIOUS PREJUDICE

One of the kinds of adverse trade effects contemplated by the SCM Agreement is "serious prejudice to the interests of a […] Member" caused by another Member's subsidies, which includes both present serious prejudice and threat of serious prejudice. The Agreement contains provisions on a number of particular forms of serious prejudice, the first two of which are based on the concept of "displacement or impedance" of trade flows. In particular, there can be displacement or impedance of a Member's exports of a "like product" into a subsidizing Member's market, or displacement or impedance of a Member's exports of a "like product" into a third country market. In both cases, a causal link needs to be established between the subsidized product and the negative effects on the exports of the like product.

The second basis of serious prejudice provided for in the SCM Agreement is significant price undercutting by a subsidized product compared with the price of a like product of another Member, in the same market (whether the market of the importing Member, a third country market, or the world market). This involves a comparison of the prices of the two products, and the establishment of a causal link between the subsidy and the price undercutting.

The third basis of serious prejudice provided for in the SCM Agreement encompasses significant price suppression or depression, or lost sales, in the same market. Price suppression is where the price competition from a subsidized product prevents the prices of the complaining Member's like product from increasing as much as they otherwise would in the absence of the subsidized competition. Price depression is where the competition from the subsidized product causes the prices of the complaining Member's like product to fall. Both of these require an analysis of price trends of the subsidized product and the like product, of the subsidy or subsidies in question, and of the other conditions of competition in the market for the goods in question. Finally, "lost sales" refers to the situation where particular contracts or sales are awarded to subsidized producers, due to subsidies, instead of to the producers of the complaining Member. Again, to establish a situation of lost sales requires detailed information as to both the subsidies and the sales contracts at issue.

The fourth basis of serious prejudice provided for in the SCM Agreement pertains only to primary products or commodities. In particular, serious prejudice can arise where the subsidy gives rise to an increase in the world market share of the subsidized primary product, compared to the average share that it held during the previous three years, and the increase follows a consistent trend over a period when subsidies have been granted. This would involve a panel obtaining information as to the size of the world market for the product in question, and of the relative market shares, and movements thereof, of the allegedly subsidizing Member and other countries. The panel also would need to obtain and analyse information about the alleged subsidy or subsidies, including the timing thereof, and the degree to which those subsidies benefited the product in question.

I.D.5. ACTIONABLE SUBSIDIES - INJURY

A second basis for action under the actionable subsidies provisions is "injury", which has the same meaning as for countervailing duty investigations. That is, this refers to material injury or threat of material injury to the domestic industry producing the product that is "like" the subsidized product imported into the territory of the

complaining Member, or to material retardation of the establishment of a domestic industry producing that product. Thus, if an allegation of injury were brought before a WTO dispute settlement panel, the panel would have to gather all of the necessary information about the condition of the domestic industry, the like product, the alleged subsidies, the allegedly subsidized product, the conditions of competition for that product in the market of the importing (complaining) Member, etc., exactly as would be required for a national countervailing duty investigation.

I.D.6. ACTIONABLE SUBSIDIES - NULLIFICATION OR IMPAIRMENT OF BENEFITS

The final kind of adverse effect provided for in the SCM Agreement is nullification or impairment of benefits accruing directly or indirectly to other Members under GATT 1994, in particular under multilateral tariff bindings. This provision reflects the reality that under certain circumstances, a subsidy provided within the territory of a Member may directly undercut the market-opening concessions that that Member has negotiated with its WTO trading partners. An example helps to illustrate the kind of situation contemplated by this provision. Suppose that Country A agrees in trade negotiations to reduce its tariff on imported barley by 10 per cent. Country B, which is a barley exporter, thus expects that its exports to Country A will increase when the tariff cut takes effect. These expectations are not realized, however. Country A, simultaneously with implementing the tariff cut, begins to subsidize its domestic purchasers of barley by an amount equal to the tariff reduction, thus removing the incentive that purchasers otherwise would have, due to the tariff reduction, to buy imported barley. These purchasers thus continue to buy the domestic barley, meaning that Country B's benefits that should have accrued from Country A's tariff reduction have been nullified or impaired by Country A's subsidy. A panel faced with a claim of nullification or impairment of benefits thus would need to obtain and analyse information on the tariff concessions involved, on the trade flows, on the alleged subsidy, and on the relationship of the subsidy to the tariff concession.

EXERCISES:

5. At present, how many categories of subsidies are there under the SCM Agreement, and what are they?

I.E. MEASURES AGAINST CERTAIN SUBSIDIES: COUNTERVAILING MEASURES

I.E.1. OVERVIEW: WHAT IS A COUNTERVAILING DUTY?

Article VI of the GATT 1994 and footnote 36 to the SCM Agreement define a countervailing duty in the following way:

> A special duty levied for the purpose of offsetting any subsidy bestowed, directly or indirectly, upon the manufacture, production or export of any merchandise.

RECALL

As discussed above, the SCM Agreement contains a two track system, therefore:

In addition to the possibility of challenging prohibited subsidies, or adverse effects caused by actionable subsidies, before a WTO dispute settlement panel, Members also have the option to use a countervailing measure on a unilateral basis, under particular, defined circumstances.

These circumstances are, in particular, where the domestic industry in the importing Member is injured by subsidized imports of a particular product. (Recall that a claim of injury, with the same meaning, also is one of the possible bases for a multilateral challenge under WTO dispute settlement.)

Although very similar to anti-dumping measures at the level of procedures, in practice countervailing duties are much less used than anti-dumping duties, for a number of reasons. A first reason is that while dumping is a practice of private parties, subsidization (the subject matter of countervailing duty investigations) is a government practice (remember, "subsidies" between private parties are not covered by the SCM Agreement). Thus, the investigating Member will have to conduct detailed inquiries into, and analyses of, the actions and measures of another government. Countervailing measures therefore are seen as more intrusive into Members' sovereignty than anti-dumping. Related to this, some Members may be reluctant to initiate a countervailing duty investigation to avoid the investigated Member from responding in kind.

Finally, in certain respects countervailing duty investigations are more complicated than anti-dumping investigations. For one thing, a great deal of calculation and estimation is involved in linking a given subsidy received by an enterprise to a particular unit of the exported good in question. Furthermore, in countervailing duty investigations, a considerable amount of information must be obtained from the government of the exporting Member, and without full co-operation from that government, there may be few if any alternative sources for the necessary information.

The provisions of the SCM Agreement applicable to countervail investigations, particularly the procedural provisions, are very similar to those on anti-dumping investigations. In this module we will focus on the points specific to countervailing measures. For the remainder, please refer to the module on anti-dumping.

Finally, because they are a border measure, countervailing measures can only be applied by an importing Member, where subsidized imports into its territory are causing injury to its domestic industry producing the like product. Any adverse effects from subsidized products in other markets (i.e., the market of the subsidizing Member, a third country market, or the world market) cannot be addressed by countervailing measures. Rather they would need to be the subject of a multilateral challenge under WTO dispute settlement procedures based on one or more of the causes of action described above (i.e., serious prejudice or nullification or impairment of benefits). (A multilateral claim of injury would not apply, as this deals with the same situation as a unilateral countervailing measure.)

I.E.2. FORMS OF COUNTERVAILING MEASURES:

As is the case for anti-dumping, the SCM Agreement provides for three kinds of countervailing measures:

- provisional countervailing duties;
- definitive countervailing duties; and
- voluntary undertakings.

PROVISIONAL COUNTERVAILING DUTIES:

Pursuant to the SCM Agreement, provisional countervailing duties may be imposed before the conclusion of an investigation, provided that there has been a preliminary affirmative finding of subsidization, injury and causation. In no case, however, can such provisional duties be applied until at least sixty days have elapsed from the date of initiation of the investigation. Furthermore, provisional countervailing duties must be limited to as a short a period as possible, and under no circumstances can they be applied for longer than four months.

DEFINITIVE COUNTERVAILING DUTIES:

Definitive duties can only be imposed on the basis of a final determination in an investigation. In particular, before it can apply a definitive duty, the importing Member must have initiated and conducted an investigation in full conformity with the applicable provisions of the SCM Agreement, and in the investigation it must have arrived at affirmative final determinations of subsidization, injury and causation.

VOLUNTARY UNDERTAKINGS:

Voluntary undertakings represent an alternative to definitive duties. In particular, a countervailing duty investigation can be suspended without the imposition of countervailing duties if the Member and/or exporter being investigated gives the investigating Member a satisfactory voluntary undertaking under which:

- the government of the exporting Member agrees to eliminate or limit the subsidy or to take other measures concerning its effects; and/or
- the exporter agrees to revise its prices so that the investigating authorities are satisfied that the injurious effect of the subsidy is eliminated.

I.E.3. RULES ON THE APPLICATION OF COUNTERVAILING MEASURES

IN BRIEF

The **SCM Agreement** sets forth certain substantive requirements that must be fulfilled in order to impose a countervailing measure, as well as detailed procedural requirements regarding the conduct of a countervailing investigation and the imposition and maintenance in place of countervailing measures. A failure to respect either the substantive or procedural requirements can be taken to dispute settlement.

IN DETAIL

SCM Agreement, PART V

Article 10 (Application of Article VI of GATT 1994)

Members shall take all necessary steps to ensure that the imposition of a countervailing duty[36] on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement. Countervailing duties may only be imposed pursuant to investigations initiated and conducted in accordance with the provisions of this Agreement and the Agreement on Agriculture.

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[36] The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise, as provided for in paragraph 3 of Article VI of GATT 1994.

GATT 1994, Article VI:3

No countervailing duty shall be levied on any product of the territory of any contracting party imported into the territory of another contracting party in excess of an amount equal to the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product in the country of origin or exportation, including any special subsidy to the transportation of a particular product. 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, upon the manufacture, production or export of any merchandise.

As is the case for anti-dumping, once the conditions set forth in the WTO rules are fulfilled, the importing Member has the legal right to apply a countervailing measure at its border in respect of the investigated imports. In other words, it does not need to seek approval from the WTO membership.

SUBSTANTIVE RULES

Similar to anti-dumping, a Member cannot impose a countervailing measure unless it determines that three elements are present:

- subsidized imports;
- injury to a domestic industry; and
- a causal link between the subsidized imports and the injury.

The concepts of *injury* and *causal link* in anti-dumping investigations have almost the same meaning in the countervail context.

The key difference between anti-dumping and countervailing measures, of course, is that for a countervailing measure, the imports in question must be subsidized. In this regard, the investigating authorities will need to collect detailed information about the alleged subsidies, to determine whether in fact these measures involve a financial contribution by a government or public body, whether they confer a benefit, and whether they are specific. If these conditions are fulfilled, the authorities will then need to determine the extent to which the subsidies in question can be attributed to the particular product under investigation. This will involve calculating the total amount of the subsidy, and then allocating or apportioning that subsidy amount over all of the products that it benefits, so that only the amount attributable to the investigated product will be taken into account in the investigation.

RECALL

> The definition of a countervailable (actionable) subsidy contains four basic elements: (i) a financial contribution (ii) by a government or any public body within the territory of a Member (iii) which confers a benefit, and (iv) which is specific.

The analysis of these four factors will have to be performed separately for each programme, measure, incentive, etc. being investigated.

Let's suppose that on the basis of such an analysis, the authority determines that programmes A, B and C are specific subsidies. The next step is to quantify the subsidy amount under each one. The SCM Agreement does not require any particular methodology for quantifying the amount of a subsidy. It does provide certain basic guidelines to be followed in respect of four different types of subsidies in order to calculate the subsidy amount in terms of the "benefit to the recipient". All of these guidelines are based on a comparison of the terms on which the government makes the financial contribution with the terms that the recipient could obtain on the market. This of course is consistent with the "benefit" element in the subsidy definition itself.

The four types of subsidies for which such guidance is provided are: (1) government equity infusions - to be compared with the "usual investment practice" of private investors in the territory of the Member involved: the benefit is the amount of any overpayment by the government; (2) government loans - what the recipient actually pays to be compared with what it would pay on a comparable commercial loan that the recipient could actually obtain on the market: the benefit is the amount of underpayment by the recipient; (3) government loan guarantees - what the recipient actually pays on the loan with the guarantee to be compared with what it would pay on the loan in the absence of the guarantee: the benefit is the amount of underpayment by the recipient; and (4) government provision of goods or services, or government purchases of goods - the

comparison is between what the recipients pays for the goods or services it buys from the government, or what it receives for the goods it sells to the government, and the prevailing market conditions in the country of provision or purchase of the goods or services, taking into account price, quality, availability, marketability, transportation and other conditions of purchase or sale: the benefit is the amount of underpayment to the government (where the government provides goods or services) or overpayment by the government (where the government purchases goods).

With respect to the amount of countervailing duty that can be imposed on subsidized imports, the SCM Agreement (in Article 19.4) sets forth two requirements:

(1) that no countervailing duty can be levied on an imported product in excess of the amount of the subsidy found to exist; and

(2) that the subsidy amount is to be expressed as an amount of subsidization per unit of the subsidized and exported product.

Thus, in the first place, no countervailing duty can ever be for an amount greater than the amount of the subsidy. (In this respect, the SCM Agreement, like the AD Agreement, expresses a preference (not an obligation) for applying a "lesser duty" if that would be sufficient to remove the injury caused by the subsidized imports.)

Furthermore, these rules make clear that finding an absolute amount of subsidization received by an enterprise is not necessarily the end of the calculation process. Rather, that total subsidy amount will need somehow to be translated into a per unit or *ad valorem* amount on the particular investigated product, which in turn will form the basis of the countervailing duty.

Also, like anti-dumping measures, countervailing measures are not of infinite duration. Rather, the SCM Agreement provides that such measures can be kept in place only for as long as and to the extent necessary to counteract subsidization which is causing injury. In this regard, the SCM Agreement contains similar provisions to those of the Anti-dumping Agreement regarding expiry or sunsetting of measures, as well as regarding changed circumstances, and the related reviews.

Let's look at some subsidy calculations in a hypothetical countervailing duty investigation:

I.E.4. ILLUSTRATION 2

Company A	***Hot rolled coils (USD250/MT)*** ←	***Private Steel Co.***
Company A	**Hot rolled coils** (USD200/MT) ←	**Gov't Owned Steel Co.**
Subsidy amount	**Amount 50USD/MT**	

In this example, we have a private company – called Company A – that needs hot rolled coils to make tubes. In this country, there are two steel producers: a private company called "Private Steel Co." and a company owned by the state "Gov't Owned Steel Co.", which for purposes of this example we assume to be a "public body" within the meaning of the SCM Agreement.

Company A asks for a price quote. For the technical characteristics, credit and delivery terms, etc. requested, "Private Steel Co." offers hot rolled coils to Company A at USD250/MT. At the same time, "Gov't Owned Steel Co." offers identical hot rolled coils on identical credit and delivery terms to Company A, but for the price of USD200/MT. The reason for this price difference is that the government wants Company A to be able to produce tubes at competitive prices. No other company is granted such a preferential price.

The first step would be to determine whether this programme, measure, incentive, etc. constitutes a subsidy. The answer is: yes, to the extent that Company A buys any hot rolled coils from the government steel company. There is a financial contribution in the form of government provision of goods, and it confers a benefit because the price of the goods provided by the government is lower than the price that Company A would have paid for goods purchased from the private company. The measure also is specific because it only benefits Company A.

The second step is to quantify the amount of the subsidy, per unit or *ad valorem*, that is attributable to the investigated product. In this example, this calculation is relatively simple, as the subsidy itself is provided on a per unit basis, namely USD50/MT, which is the difference between the price paid to "Gov't Owned Steel Co." for the hot rolled coil and the price charged by "Private Steel Co." If we assume for simplicity that that every tonne of tubing produced uses exactly one tonne of coil (i.e., that there is no waste factor), a countervailing duty of USD 50/MT, or the *ad valorem* equivalent, could be applied by the importing Member on the imported tubing.

A different kind of subsidy could pose more calculation complexities, however. Let's assume that Company A also receives a loan from the government, and that the annual amount of the benefit under the loan (i.e., the difference between what Company A pays on the loan and what it would pay on a comparable commercial loan) is USD10,000. How do we translate this subsidy amount into a per unit or *ad valorem* amount on imports of tubing? First we need to know which products of Company A's product line benefit, in a theoretical sense, from the subsidy. Let's assume that the subsidy is for export enhancement, so it is contingent on export performance, i.e., it is an export subsidy. Given this, it is reasonable to attribute the subsidy benefits to Company A's total exports of all products. Because Company A produces and exports a number of different products, we must spread these benefits equally over all of these exports, not just exports of the investigated tubing. Let's further assume that Company A's total export sales during the one-year period of investigation total USD100,000. The *ad valorem* subsidy calculation would be:

$$\frac{USD10'000\ (subsidy\ amount)}{USD100'000\ (total\ export\ sales)} = 10\%\ ad\ valorem$$

How then would the investigating authority determine the maximum countervailing duty that it could apply? It would have to sum the subsidy amounts on the product from the different investigated subsidies. This in turn would imply putting these amounts on the same basis. In our example, this would mean that the investigating authority would need to calculate the *ad valorem* equivalent of the USD50 per metric tonne subsidy amount on the hot rolled coils, so that this could be added to the 10 per cent from the subsidized loan, to arrive at the maximum *ad valorem* countervailing duty that could be applied to the imported tubing. To calculate the *ad valorem* subsidization of the tubing from the hot rolled coils, we will need to have a value per ton, say its selling price, for the tubing. Let's assume that this is USD 400.

The following example presents the calculation of the total ad valorem subsidization of the investigated tubing:

Calculation of the total ad valorem subsidization of the investigated tubing	
Subsidy 1: USD 50 per MT of tubing. Selling price of tubing = USD 400.	USD 50 ÷ USD 400 = 12.5% *ad val.*
Subsidy 2:	10% *ad val.*
Total ad valorem subsidization of tubing exported by Company A:	**12.5% + 10%= 22.5%**

The maximum level of countervailing duty that could be applied to imported tubing produced by Company A thus is 22.5% *ad valorem.*

PROCEDURAL RULES

As stated above, the procedural rules in the SCM Agreement covering countervailing duty investigations and application of measures are very similar to those contained in the Anti-Dumping Agreement. The following main differences should be noted:

- Consultation requirement: As soon as possible after an application is accepted, and in any event before the initiation of any investigation, Members the products of which may be subject to such investigation must be invited for consultations with the aim of clarifying the situation and arriving at a mutually agreed solution.
- *De minimis* subsidization, negligible import volumes: The SCM Agreement contains its own levels for *de minimis* subsidization and negligible import volumes. Countervailing duty investigations and measures must be terminated immediately in cases where the amount of a subsidy is *de minimis* (generally, less than 1% *ad valorem*) or where the volume of subsidized imports, actual or potential, or the degree of injury, is negligible. Separate thresholds are established for developing country Members (as discussed below)..
- Undertakings: These are not limited to "price" undertakings by the exporting companies, as in the Anti-Dumping Agreement. Rather, the SCM Agreement also contemplates undertakings under which the government of the exporting Member agrees to eliminate or limit the subsidy or to take other measures concerning its effects.
- Other: The SCM Agreement does not contain specific rules on issues such as sampling of exporters, duty collection systems, or individual rates. Nor, unlike the Anti-Dumping Agreement, does it contain an Annex setting forth the detailed rules on the use of facts available (although recourse to facts available is permitted under the same circumstances as apply in the case of anti-dumping).

EXERCISES:

6. What can a Member do if it believes that its interests have been harmed by the subsidization of another Member?

7. What three determinations does a Member need to make in order to be able to apply a countervailing measure?

8. If a company that produces 20 products receives a general subsidy to its overall operations, can a Member importing one of those products, and conducting a countervailing duty investigation on that product, treat the entire subsidy as a subsidy to the imported product that it is investigating?

I.E.5. ILLUSTRATION 3

Let's look at another illustration:

Let's assume that over the years the watch industry of Member A has begun to compete strongly with that of Member D.

The Government of Member D, concerned over the declining competitiveness of its national industry, grants a subsidy of 5 billion Crowns to one of its companies, VanWatch Ltd. Because of the subsidy, VanWatch is able to buy new state-of-the-art equipment that allows it to produce more watches at a price 20% lower than previously, while maintaining high quality. VanWatch begins to export these watches to Member A.

Pursuant to the SCM Agreement, the Government of Member A conducts a countervailing duty investigation. TickTock, a watchmaker from Member A, produces evidence that it is losing market share because of the now cheaper Member D watches being exported by VanWatch.

Once the Government of Member A determines that there is indeed subsidization, that the domestic industry has been injured, and that there is a link between the injury and the subsidy, the Government of Member A has to determine the level of the countervailing duty. The countervailing duty cannot be more than what is necessary to counteract or "offset" the subsidization from the Government of Member D.

Member A thus would need to allocate on a reasonable basis the total subsidy amount of 5 billion Crowns to the products produced by VanWatch that are benefited by the subsidy, in this case, the products produced on the new equipment purchased with the subsidy proceeds. In addition, given that the subsidy is for production equipment (i.e., capital equipment) with presumably a multi-year productive life, Member A would need to consider the timeframe over which the subsidy could be seen as benefiting VanWatch. In this regard, Member A might follow the theory that, while the subsidy is given all at once, the benefits it confers will persist over the full useful life of the assets that VanWatch acquired with the subsidy. Thus, rather than assuming that all of the benefits were "consumed" instantaneously by VanWatch when it received the subsidy, the idea would be that those benefits would be gradually used up as the equipment itself was used up.

As a simple example, assume that the useful life of the production equipment acquired with the subsidy is 15 years. This would give a per year subsidy amount of 333,333,333 Crowns (not taking into account any adjustment for time value of money). Assuming that VanWatch's annual sales turnover of watches produced on this equipment was 3 billion Crowns, the *ad valorem* subsidy amount on those watches would be 11.1 per cent.

It is possible that this same subsidy granted to VanWatch, which is causing injury to the domestic industry of Member A via the subsidized imports into Member A's territory,, also could have the effect of reducing Member A's exports to the market of Member D. For example, in addition to exporting, VanWatch might also sell a considerable number of watches into its own home market (the territory of Member D), and the subsidy to VanWatch would make it difficult for Member A to maintain its market share there. Clearly, Member A's countervailing measure, on subsidized imports into its own territory, would not have any impact on its exports to another market. However, Member A could bring a claim of displacement or impedance of its exports into the territory of the subsidizing Member (Member D) before a WTO dispute settlement panel. If Member A prevailed, Member D would have to withdraw the subsidy or eliminate the adverse effects thereof on Member A's exports.

I.F. TRANSITION RULES AND SPECIAL AND DIFFERENTIAL TREATMENT

I.F.1. DEVELOPED MEMBERS

According to Article 28.1 of the SCM Agreement, developed Members were granted a period of three years from the date on which the SCM Agreement entered into force (i.e., through 31 December 1997), to phase out any existing subsidies that fell into the prohibited category (i.e. export subsidies and import substitution subsidies). Such subsidies had to be notified to the SCM Committee within 90 days of the date of entry into force of the SCM Agreement.

I.F.2. MEMBERS IN TRANSFORMATION FROM CENTRALLY-PLANNED TO MARKET ECONOMIES

Members in transformation from centrally-planned to market, free-enterprise economies were given seven years from the date of entry into force of the WTO Agreement (i.e., through 31 December 2001) to phase out their existing prohibited subsidies of both types (export subsidies and import substitution subsidies). To be able to take advantage of this transition period, these Members had to notify the subsidies in question to the SCM Committee not later than two years after the entry into force of the WTO Agreement (i.e., by 31 December 1996).

During the seven-year transition period, the actionable subsidies of Members in transformation to market economies also were exempted from certain disciplines on actionable subsidies.

I.F.3. DEVELOPING MEMBERS

The SCM Agreement recognizes that subsidies may play an important role in economic development programmes of developing Members, and in this respect provides extensive special and differential treatment for those Members.

In particular, the SCM Agreement establishes a unique sub-categorization of developing Members for purposes of transition rules and other S&DT provisions pertaining to prohibited subsidies. The Agreement also provides for S&DT in respect of actionable subsidies, and for certain provisions related to the use of countervailing measures in respect of developing Members' exports.

S&DT - EXPORT SUBSIDIES

On export subsidies, the SCM Agreement breaks developing Members into three sub-categories: least developed ("LDC") Members; certain listed other developing Members with GNP per capita below USD1,000 per annum; and all other developing Members. Generally speaking, the lower the level of the developing Member's development as reflected in these categories, the more flexible the rules regarding the use of export subsidies.

First, LDC Members are not subject to the prohibition on export subsidies for as long as they remain designated as LDCs by the United Nations. (This provision is contained in paragraph (a) of Annex VII to the SCM Agreement). Second, certain listed Members with GNP per capita below USD1000 per year are not subject to the prohibition on export subsidies until their GNP per capita reaches USD1000. (This provision is contained in paragraph (b) of Annex VII to the SCM Agreement. Finally, all other developing Members had a period of eight years from the entry into force of the SCM Agreement to phase out their export subsidies. These other developing Members had the possibility to seek extension of this eight-year phase-out period, by agreement of the SCM Committee.

Certain decisions relative to the S&DT provisions on export subsidies were taken in the Doha Ministerial Decision on Implementation-Related Issues and Concerns. First, concerning the GNP per capita threshold applicable to Members listed in Annex VII(), Ministers decided that the listed Members would remain exempt from the prohibition on export subsidies until their GNP per capita had reached USD1000 calculated in constant 1990 US dollars for three consecutive years. They further decided that if the GNP of a Member that had already surpassed that threshold fell back below USD1000, that Member could re-introduce export subsidies. Second, concerning the possibility to extend the eight-year transition period applicable to the other developing Members, Ministers also decided on a package of "fast-track" extension procedures for certain developing Members with small economies and small shares of world trade. Under these procedures, these Members obtained extensions on a streamlined basis, subject to standstill and transparency requirements. The extension package was renewed, with important modifications, in 2007. Pursuant to the renewal package, the small developing Members with the extensions must completely eliminate their export subsidies not later than the end of 2015.

TIP

It is important to note that even where a developing Member is exempt from the prohibition on export subsidies via any of the above-discussed provisions and mechanisms, its export subsidies remain actionable. That is, they can be subject to countervailing measures, as well as to multilateral claims of adverse effects (serious prejudice, injury, or nullification or impairment).

S&DT - IMPORT SUBSTITUTION SUBSIDIES

The special and differential treatment provisions of the SCM Agreement in respect of the other category of prohibited subsidies (import substitution subsidies) are considerably simpler than those for export subsidies. Furthermore, these provisions have now expired for all developing Members, including LDCs.

In particular, LDC Members had a flat, non-extendable period of eight years in which to fully eliminate their import substitution subsidies. All other (i.e., non-LDC) developing Members were given five years to fully eliminate their import substitution subsidies. These periods thus expired at the end of 2002 and 1999, respectively.

S&DT - ACTIONABLE SUBSIDIES

Developing Members also benefit from certain special treatment in respect of the disciplines on actionable subsidies. First, regarding adverse effects, the actionable subsidies of these Members cannot be subject to

multilateral claims of serious prejudice, but only to claims of injury or nullification or impairment of benefits. As noted above, only the prohibited subsidies of these Members could potentially be subject to serious prejudice claims (in theory this would probably only occur where a developing Member remained exempt from the prohibition due to one of the transition rules or mechanisms discussed above.) Furthermore, actionable subsidies directly linked to a developing Member's privatization programmes are exempt from adverse effects challenges, if they meet certain conditions.

S&DT - COUNTERVAILING MEASURES

Finally, although all specific subsidies of developing Members are fully countervailable, these Members nevertheless benefit from certain S&DT in this area as well. In particular, the *de minimis* subsidization threshold applicable to exports of a developing Member is 2 per cent (compared with 1 per cent for developed Members' exports); and the negligible imports thresholds also are higher for developing Members' exports than for developed Members' exports. In other words, in in a countervailing duty investigation of a developing Member's exports it is determined that the *ad valorem* amount of subsidization of the product is 2 per cent or less, the investigation must be terminated immediately. By contrast, if the investigated exporter were a developed country, the investigation could continue, and a countervailing measure eventually could be applied, given the lower *de minimis* threshold applicable to developed Members' exports.

IF YOU WANT TO KNOW MORE...

Definition of a "developing country" in the WTO

How is a Member designated as "developing" at the WTO?

In fact, there are no official agreed WTO definitions or lists of "developing" and "developed" Members. Instead, Members announce for themselves whether they are "developed" or "developing". Other Members do have the possibility to challenge a given Member's decision to make use of developing Member special and differential treatment provisions. To date, however, no such challenges have been raised.

I.G. NOTIFICATIONS

I.G.1. SUBSIDIES

The SCM Agreement obliges Members to submit a variety of notifications to the SCM Committee. Except where a notifying Member has specifically requested to the contrary, all notifications are issued as unrestricted documents and are fully accessible to the public upon their circulation to Members.

TIP

All notifications are available through the WTO Web site. The discussion below of some of the main types of notifications submitted to the SCM Committee, and of the document series in which they may be located, is intended to assist in the identification and retrieval of these documents by interested Members and others.

NOTIFICATIONS OF SPECIFIC SUBSIDIES.

Article 25 of the SCM Agreement requires that all Members periodically submit new and full notifications of all of their specific subsidies.

The notification obligation covers all specific subsidies related to goods, in all sectors (including agriculture), and provided by all levels of government (national, regional, state or provincial, local, etc.). Members that consider that they provide no specific subsidies are required to make a "nil" notification to that effect.

Importantly, the SCM Agreement provides explicitly that submitting a notification in no way constitutes an admission that the measure is a specific subsidy. In particular, the SCM Agreement states that notifying does not prejudge a measure's legal status under GATT 1994 and the SCM Agreement, its effects under the SCM Agreement, or the nature of the measure itself. In practical terms, this means among other things that the fact that a measure is notified under the SCM Agreement cannot be used as evidence, either in a countervailing duty investigation or in a WTO dispute, that that measure is a specific subsidy. Instead, such a measure would need to be analysed fully under the provisions of the SCM Agreement to determine if it fulfilled all of the pertinent definitional requirements contained therein. This protection of a measure from legal characterization based upon its having been notified is intended to encourage Members to err on the side of inclusiveness in their notifications, in the interests of transparency.

A format for notifying measures under the SCM Agreement can be found in document G/SCM/6/Rev.1.

The document sets forth information that must be provided in a Member's notification:

INFORMATION TO BE PROVIDED

1. Title of the subsidy programme, if relevant, or brief description or identification of the subsidy.
2. Period covered by the notification. The period to be covered by the notification should be the most recently completed calendar or fiscal year. In the latter case, the start and end dates of the fiscal year should be specified.
3. Policy objective and/or purpose of the subsidy.
4. Background and authority for the subsidy (including identification of the legislation under which it is granted).
5. Form of the subsidy (i.e., grant, loan, tax concession, etc.).
6. To whom and how the subsidy is provided (whether to producers, to exporters, or others; through what mechanism; whether a fixed or fluctuating amount per unit; if the latter, how determined).
7. Subsidy per unit, or in cases where this is not possible, the total amount or the annual amount budgeted for that subsidy (indicating, if possible, the average subsidy per unit in the previous year). Where provision of per unit subsidy information (for the year covered by the notification, for the previous year, or both) is not possible, a full explanation.
8. For the information cited in items 3 to 7 above, the notification does not necessarily have to have an independent heading corresponding to each item, and may provide information on multiple items in one heading (e.g. provide information on items 3 and 4 under one heading). In this case, the notification must clearly specify what items are covered by which heading.
9. Duration of the subsidy and/or any other time limits attached to it, including date of inception/commencement.

10. Statistical data permitting an assessment of the trade effects of the subsidy. The specific nature and scope of such statistics is left to the judgement of the notifying Member. To the extent possible, relevant and/or determinable, however, it is desirable that such information include statistics of production, consumption, imports and exports of the subsidized product(s) or sector(s):

    (a) for the three most recent years for which statistics are available;

    (b) for a previous representative year, which, where possible and meaningful, should be the latest year preceding the introduction of the subsidy or preceding the last major change in the subsidy.

New and full subsidy notifications are, by understanding of the SCM Committee, to be provided every two years. Also by understanding of the SCM Committee, compliance with this requirement is generally taken to be sufficient also to comply with the SCM Agreement's provisions on updating notifications.

TIP

Subsidy notifications are circulated in the G/SCM/N series, with a unique number assigned to the series for each notification year. For example, the 2011 new and full notifications are contained in the series G/SCM/N/220/…, with the notifying Member identified by its three- or four-letter ISO country code. Thus, Chile's 2011 new and full notification is contained in document G/SCM/N/220/CHL. In addition, there may be corrections, revisions, and supplements to any given notification, so a complete notification may include several documents.

WORLD TRADE ORGANIZATION

G/SCM/N/220/CHL
27 July 2011
(11-3812)

Committee on Subsidies and Countervailing Measures

Original: Spanish

SUBSIDIES

New and Full Notification Pursuant to Article XVI.1
of the GATT 1994 and Article 25 of the SCM Agreement

CHILE

The following notification, dated 25 July 2011, is being circulated at the request of the delegation of Chile.

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I. TAX CREDIT FOR INVESTMENT IN THE PROVINCES OF ARICA AND PARINACOTA (REGION I)

Title

Tax Credit for Investment in the Provinces of Arica and Parinacota (Region I).

Period

To July 2011.

I.A.1 Objectives

To reverse the declining economy of the provinces of Arica and Parinacota, making use of both their advantageous geographical position for trade purposes and their tourist attractions, strengthening entrepreneurship and consolidating Arica as an inter-ocean corridor.

Background and authority

Background: Arica and Parinacota, as outlying provinces, are at a disadvantage in relation to the development of the rest of the country.

Authority: Law No. 19.420, published in the Official Journal of 23 October 1995, amended by Laws Nos. 19.478 (Official Journal of 24 October 1996) and 19.669 (Official Journal of 5 May 2000). Decree having Force of Law (DFL) No. 1 of the Ministry of Finance, published in the Official Journal of 11 September 2001, contains the revised, coordinated and consolidated text of Law No. 19.420. The latest amendment to this Law was by means of Law No. 20.512 of 7 May 2011.

Form of the subsidy

Tax credit in the form of a tax allowance.

To whom and how is the subsidy provided

This incentive is for taxpayers with investment projects in the following amounts for the periods below:

1. In the province of Arica:

   (a) 2008 and 2009: 1,000 UTM ($38,173,000, equivalent to US$81,614)[1];
   (b) 2010: 1,500 UTM ($57,259,000, equivalent to US$122,420);
   (c) 2011: 2,000 UTM ($76,346,000, equivalent to US$163,227).

2. In the province of Parinacota, investments must amount to more than 1,000 UTM ($38,173,000, equivalent to US$81,614).

The period for eligibility is up to 31 December of each year.

The beneficiaries are entitled to a tax credit of 30 per cent of the value of certain non-convertible assets, namely, buildings, machinery and equipment, including immovable property intended primarily for commercial exploitation for tourist purposes, directly tied in with the production of goods or the supply of services of the taxpayer's business or activity, purchased new or finished in the financial year.

For investment operations carried out in Parinacota, the tax credit is 40 per cent. The same percentage is applied to investments made in Arica in immovable property intended primarily for commercial exploitation for tourist purposes, and identified as being of particular interest by the Director of the National Tourism Service.

Taxpayers are also eligible for this credit if they invest in the construction of buildings for use as offices or dwellings, whether or not they include business premises, car parks or shops, consisting of more than five units, in places specified in the Law, with a built area of not less than 1,000m2 and completed or built during the financial year.

The taxes are forgiven by deducting the credit from the first-category tax payable as from the trading year of the purchase or construction of the property.

I.A.2 Amount of the subsidy

In 2011, the tax credit, estimated in terms of tax revenue forgone, is estimated at Ch$1,000 million (equivalent to US$2,137,992).2

I.A.3 Duration

This incentive became effective, retroactively, as from 1 January 1995. The period for eligibility is up to 31 December 2012.

The benefit will apply only in regard to assets incorporated in the investment project on any of the above-mentioned dates on which the benefit is still effective, although the credit may be recovered up to the year 2034.

I.A.4 Statistical data

No data available.

[1] UTM at May 2011: $38,173. *Source*: Central Bank.

Average exchange rate of the Chilean peso to the US dollar in May 2011: $467.73. *Source*: Central Bank.

[2] Average exchange rate of the Chilean peso to the US dollar between January and July, $580.62. Source: Central Bank.

II. EXEMPTION FROM FIRST-CATEGORY TAX UNDER THE INCOME TAX LAW ON FISCAL-YEAR PROFITS OF MANAGEMENT COMPANIES AND USERS IN THE FREE ZONES IN THE CITIES OF IQUIQUE (REGION I) AND PUNTA ARENAS (REGION XII)

II.A.1 Title

Exemption from first-category tax under the Income Tax Law on fiscal-year profits of management companies and users in the free zones in the cities of Iquique (Region I) and Punta Arenas (Region XII).

II.A.2 Period

To July 2011.

II.A.3 Objectives

To stimulate the economic development of Region I and Region XII, so as to form an attractive area for investment, economic activity, settlement, growth and sovereignty.

II.A.4 Background and authority

Background: These areas, because of their location and geographical features, are at a disadvantage in relation to the development of the rest of the country.

Authority: The legal authority is contained in Ministry of Finance Decree No. 341, published in the Official Journal of 8 June 1977, the revised, coordinated and consolidated text of which is set forth in Decree having Force of Law No. 2 of the Ministry of Finance, published in the Official Journal of 10 August 2001.

II.A.5. Form of the subsidy

In practice, the subsidy is a temporary financial benefit. It is not equal to the overall amount of the tax exemption.

Indeed, the 1984 Income Tax Law provided for a first-category tax (on companies) and a second category tax (on natural persons). Accordingly, the owners of an enterprise may discount the amount of first-category tax paid (15 per cent on a company's annual profits) from the amount payable as second-category tax (a progressive tax that represents a percentage of withdrawn profits).[3]

Since the companies concerned benefit from first-category tax exemption, management companies and users in free zones have nothing to discount from their second-category tax and must therefore pay the full amount of this tax. The benefit of the exemption therefore amounts strictly to the financial cost not incurred for the period between the time when the first-category tax became payable and the time (or times) when profits are withdrawn and the corresponding second-category tax becomes payable.

II.A.6 To whom and how is the subsidy provided

This incentive is for management companies and users (all legal persons) in the free zones of Iquique (Region I) and Punta Arenas (Region XII). They must meet the requirements established by the Ministry of Finance and the Ministry of the Economy, Development and Reconstruction, under contracts containing conditions freely agreed on with the interested party.

These benefits also apply to manufacturing companies already established or setting up in Arica and manufacturing companies in the Alto Hospicio district in Iquique.

Beneficiaries are exempt from the first-category tax under the Income Tax Law on fiscal-year profits.

II.A.7 Amount of the subsidy

There are no official calculations of tax revenue forgone.

II.A.8 Duration

This incentive took effect on 25 June 1975 for Iquique and Punta Arenas and on 10 December 1976 for Arica. In both cases it is of indefinite duration.

[3] The level of income considered for the second-category tax includes income other than withdrawn profits, such as salaries, etc.

II.A.9 Statistical data

No statistical calculation has been made to assess the trade effects of the subsidy.

III. FUND FOR THE PROMOTION AND DEVELOPMENT OF REMOTE AREAS

III.A.1 Title

Fund for the Promotion and Development of Remote Areas.

III.A.2 Period

To July 2011.

III.A.3 Objectives

To contribute to the development of the disadvantaged regions of Tarapacá, Aysén, Presidente Carlos Ibáñez del Campo, Magallanes and the Chilean Antarctic territories and the provinces of Chiloé and Palena, by providing assistance to small and medium-sized investors wishing to invest or reinvest in production in these remote regions.

III.A.4 Background and authority

Background: Being in outlying regions and provinces, these areas are at a disadvantage in relation to the development of the rest of the country.

Authority: This fund was created by virtue of Articles 38 and 39 of Decree Law No. 3.529 of the Ministry of Finance, published in the Official Journal of 6 December 1980. Decree No. 15 of the Ministry of Finance, published in the Official Journal of 20 April 1981, lays down the terms and conditions of this fund.

Decree having Force of Law No. 15 entered into effect pursuant to a budgetary note (No. 50-01-02-33-01-002) incorporated in the Public Sector Budget Law for 2011 (Law No. 20481).

III.A.5 Form of the subsidy

Direct transfer.

III.A.6 To whom and how is the subsidy provided

Funds may only be accorded for investments by small and medium-sized investors, and producers of goods and services in the sectors of construction, machinery, equipment, special animal feed and small-scale fishing. The annual amount of individual investment or reinvestment must not exceed 50,000 UF (*unidades de fomento* - Chilean inflation-indexed monetary units)[4], equivalent to US$2,327,630. Funds granted under this programme may not be accepted together with any other benefit granted by the Government of Chile for the same goods or services.

This fund makes a contribution of 20 per cent of the cost of investment or reinvestment made up to 31 December 2011. The benefit is renewed from year to year under the Budget Law.

III.A.7 Amount of the subsidy

For 2011, the Budget Law has estimated the maximum amount to be paid out at Ch$1,500 million (equivalent to US$3,206,988).

III.A.8 Duration

This facility is available until 31 December 2011. The benefit is renewed from year to year under the Budget Law.

III.A.9 Statistical data

No data available.

[4] Average value of the UF at May 2011: $21,774.

NOTIFICATIONS OF INCONSISTENT SUBSIDIES

As discussed above, the SCM Agreement required developed Members and Members in the process of transformation to market economies to notify their pre-existing subsidies inconsistent with the SCM Agreement (i.e., export subsidies and import substitution subsidies), in order be able to use the applicable transition periods for those subsidies. These transition periods have now expired.

Members' notifications of these types can be found in the document series G/SCM/N/2/… (for notifications by developed Members) and G/SCM/N/9/… (for notifications by Members in transformation to market economies).

NOTIFICATION RULES APPLICABLE TO DEVELOPING MEMBERS:

New and full subsidy notifications

There is no special and differential treatment accorded to developing Members in respect of the requirement to notify specific subsidies. All Members face uniform rules as to the content and frequency of such notifications. Developing Members' export subsidies and import substitution subsidies, during the periods when they are or were exempt from prohibition, were subject to notification by virtue of the "deemed" specificity of these subsidies.

Export subsidy notifications related to extensions of the phase-out period

As discussed above, certain developing Members obtained extensions of the phase-out period for certain export subsidies. Pursuant to the extension decisions, as part of the terms and conditions for annual renewal of these extensions during the agreed period, the Members involved must submit annual notifications as to the legal basis and operation of these subsidies, to ensure full transparency about the subsidies, as well as compliance with the agreed standstill package). In addition, the Members in question have been required to submit information confirming that the beneficiaries of the subsidies have been notified that export subsidies will cease as of the end of 2015. They also have had to provide notifications as to their plans for bringing these export subsidy programmes into conformity with the SCM Agreement by that date.

The 2011 notifications were circulated in the G/SCM/N/226/… series. Written questions and answers concerning these notifications can be found in the G/SCM/Q3/… series.

Privatization subsidies

As discussed above, certain privatization subsidies of developing Members can be exempted from multilateral adverse effects claims if certain conditions are met. One of these is that the subsidies in question must be notified. Notifications made pursuant package). In addition, the Members in question have been required to submit information confirming that the beneficiaries of the subsidies have been notified that export subsidies will cease as of the end of 2015. They also have had to provide notifications as to their plans for bringing these export subsidy programmes into conformity with the SCM Agreement by that date.

The 2011 notifications were circulated in the G/SCM/N/226/… series. Written questions and answers concerning these notifications can be found in the G/SCM/Q3/… series.

I.G.2. COUNTERVAILING MEASURES LEGISLATION AND ACTIONS

The SCM Agreement requires a number of notifications pertaining to countervailing measures. These include legislative notifications as well as certain notifications relating to countervailing actions taken.

COUNTERVAILING DUTY LEGISLATION

Members are required to notify to the SCM Committee the full text of their domestic laws and regulations relating to countervailing measures, and any changes to these laws and regulations. Members that have no countervailing duty laws or regulations are required to make a nil notification to that effect. The legislative notifications can be found in WTO document series G/SCM/N/1/... .

TIP

Subsequent to the initial notification of a full legislative text, there may be further notifications, containing corrections, amendments, revisions, supplements, or entirely new texts. Thus, getting a complete understanding of a Member's legislation pertaining to countervailing measures may require a review of several documents. Furthermore, where a completely new legislation and/or regulation entirely replaces one that has previously been notified, a new document number is assigned. For example, Fiji's initial (nil) legislative notification was circulated in document G/SCM/N/1/FJI/1. Subsequently, Fiji enacted and notified countervailing measures legislation, and this was circulated in document G/SCM/N/1/FJI/2. Members' written questions and answers pertaining to legislative notifications are circulated in the G/SCM/Q1/... series.

SEMI-ANNUAL REPORTS OF COUNTERVAILING ACTIONS

The SCM Agreement requires each Member to notify twice per year all of its countervailing actions taken during the reporting period, as well as a list of all of its countervailing measures in force. The format for these semi-annual reports can be found in document G/SCM/2/Rev.1. Members that have taken no countervailing action during the period in question are required to make a nil notification to that effect. Each group of semi-annual reports pertaining to a given six-month period has its own document series, with each report identified by the submitting Member's three-letter ISO country code. For example, the semi-annual reports for the first semester of 2011 can be found in document series G/SCM/N/228, and the report of the United States is document G/SCM/N/228/USA.

NOTIFICATIONS OF PRELIMINARY AND FINAL COUNTERVAILING ACTIONS

The SCM Agreement also requires Members to notify on an *ad hoc* basis as they take these actions all of their preliminary and final countervailing actions, . The notifications can take the form either of the full text of a Member's public notice of the action in question, or a summary following the format set forth in document G/SCM/3/Rev.1.

TIP

Rather than circulating the full texts of the notifications of preliminary and final actions, the WTO Secretariat circulates on a monthly basis lists of such notifications received. The notifications themselves are kept on file and can be consulted upon request by any Member.

NOTIFICATIONS OF COMPETENT AUTHORITIES

Finally, Members are required to notify to the SCM Committee the names and contact details of their authorities that are competent to initiate and conduct countervailing investigations (if they have such authorities). Lists of these notified authorities are periodically circulated to Members, in the document series G/SCM/N/18.

I.H. DISPUTE SETTLEMENT

The SCM Agreement generally relies on the dispute settlement rules of the DSU. In addition, however, the SCM Agreement contains a number of special or additional dispute settlement rules and procedures as discussed above in the sections pertaining to multilateral subsidies disciplines. These special rules provide for, among other things, expedited procedures relative to standard DSU procedures, particularly in the case of prohibited subsidy allegations. The SCM Agreement also contains a special fact-gathering mechanism for serious prejudice claims, which can be used by a panel, at the request of a party.

I.I. THE SCM COMMITTEE

The operation of the SCM Agreement is overseen by the Committee on Subsidies and Countervailing Measures, which is composed of representatives of all WTO Members. The SCM Committee is tasked with reviewing all notifications submitted by Members. It also provides a forum where Members can discuss any issue related to the operation of the SCM Agreement.

The SCM Committee meets twice per year in regular session, and its meeting agendas tend to be similar to those of the Anti-Dumping Committee. In fact, for the review of legislative notifications, because many Members enact legislation and other legal instruments that regulate both anti-dumping and countervailing measures, one of these Committees (usually the Anti-Dumping Committee) generally conducts the primary review of these legislations, with the other Committee (usually the SCM Committee) reviewing only those elements of legislative notifications that pertain specifically to its particular subject matter. For example, where the AD Committee conducts the primary review of a given legislative notification, that review will cover all of the anti-dumping-specific provisions as well as the provisions applicable to both anti-dumping and countervailing measures. The SCM Committee will then finish the review of this notification by taking up only the provisions of that notification that pertain exclusively to countervailing measures.

The SCM Committee of course conducts its own primary review of the subsidy notifications of various types, and of the semi-annual reports and *ad hoc* notifications of countervailing actions taken.

I.J. THE PERMANENT GROUP OF EXPERTS

The SCM Agreements establishes a Permanent Group of Experts ("PGE"), the members of which are to be elected by the SCM Committee, and one of whom is to be replaced each year.

The Permanent Group of Experts is charged with three responsibilities:

1. To assist a dispute settlement panel, at the panel's request, with regard to whether a measure before the panel is a prohibited subsidy. The panel must accept without modification the conclusions reached by the PGE.

2. To provide the SCM Committee, upon request of the Committee, advisory opinions as to the existence and nature of any subsidy.

3. To consult with any Member and to provide confidential advisory opinions, upon request, as to the nature of any subsidy proposed to be introduced or currently maintained by that Member.

When the PGE was first constituted, following the entry into force of the SCM Agreement, its original members drafted a set of working procedures for how the PGE would carry out the above functions. The draft procedures were debated by the SCM Committee, but the Committee failed to reach a consensus to adopt them. The lack of working procedures almost certainly is a major reason why, in practice, the PGE has never been called upon to perform any of its statutory tasks.

EXERCISES:

9. Do or did developing countries receive any special treatment under the SCM Agreement with respect to prohibited subsidies?

10. Are developing countries that are exempt from the prohibition on export subsidies fully protected from challenge with respect to such subsidies?

III. SUMMARY

SUBSIDIES AND COUNTERVAILING MEASURES

The SCM Agreement does not prohibit Members from granting subsidies.

The SCM Agreement contains rules to determine which programmes, measures, etc. are subsidies covered by it. The SCM Agreement disciplines the use of the subsidies it covers, and regulates the actions countries can take to counter the effects of those subsidies.

The SCM Agreement is, in fact, "two agreements in one". Under its multilateral track, the SCM Agreement gives Members the right to challenge certain subsidies of other Members under the Dispute Settlement Understanding of the WTO. Under its national, or unilateral, track the SCM Agreement establishes that if certain conditions are met, a Member may carry out an investigation and impose countervailing measures on subsidized imports into its territory that are injuring its domestic industry.

For a measure to be considered a subsidy for the purposes of the SCM Agreement, it must be comprised of three elements:

- A financial contribution
- By a government or public body
- That confers a Benefit

In addition,

- Only subsidies that are "specific" are subject to the SCM Agreement.

Although the SCM Agreement initially covered three types of subsidies, only two types remain:

- Prohibited subsidies (presumed to distort international trade). These are subsidies contingent upon export performance and subsidies contingent on the use of domestic goods
- Actionable subsidies (they can be challenged if they cause certain kinds of harm to another Members trade interests)
- Recall that the non-actionable subsidy category expired at the end of 1999.

The SCM Agreement provides for three forms of countervailing measures:

- Provisional countervailing duties
- Definitive countervailing duties
- Voluntary undertakings

The imposition of any countervailing measure must fulfil the substantive and procedural requirements set forth in the SCM Agreement. Many of these requirements are similar to those contained in the Anti-Dumping Agreement. This module therefore refers to the module on the Anti-Dumping Agreement where there is overlap, and explains the differences where relevant.

Countervailing measures are subject to five-year sunsetting provisions, but can be extended on the basis of a review. They also can be subject to review to determine whether they remain necessary to prevent or remedy injury, and whether their level could be modified.

The SCM Agreement recognizes that subsidies may play an important role in economic development programmes of developing countries. The Agreement therefore contains less strict rules and disciplines on the subsidies of developing Members than those that apply to developed Members. Finally, the SCM Agreement requires Members to submit a variety of notifications to the SCM Committee. Except where a notifying Member has specifically requested otherwise, all notifications are issued as unrestricted documents and are fully accessible to the public.

PROPOSED ANSWERS:

1. No. The definition of the term "subsidy" in the SCM Agreement contains three basic elements:

   (i) a financial contribution.

   (ii) by a government or any public body within the territory of a Member.

   (iii) which confers a benefit.

   The financial contribution can take various forms, not all of them monetary. The SCM Agreement contains an exhaustive list of the type of measures that represent a financial contribution: direct transfers of funds (e.g. grants, loans, or equity infusions), potential direct transfers of funds or liabilities (e.g. loan guarantees), government revenue that is foregone (e.g. through fiscal incentives such as tax credits), the provision of goods or services, and the purchase of goods. Additionally, certain income or price support also can be a subsidy if it confers a benefit.

2. Yes. The Agreement refers to a financial contribution by a government or any public body within the territory of a Member, and therefore applies not only to subsidies provided by national governments, but also those provided by sub-national governments such as state or local governments, and by public bodies, which may include various types of entities that are not governments but that have or fulfil a public policy role. It should be noted, in this regard, that when assessing whether a subsidy is specific on a regional basis, the territory over which the granting authority has jurisdiction is the point of departure, at whatever level of government. a For instance, if the granting entity is a state government, regional specificity would exist if the subsidy were granted only to firms located in a certain part of the territory of that state, but not if it were granted to firms throughout the state.

3. Yes. As a special, temporarily exemption from tax that is in force and generally applies to all manufacturers, the measure would be a financial contribution in the form of government revenue foregone that was otherwise due. It would confer a benefit because it is essentially a grant - something for nothing. And it would be specific because access to it is limited to a single industry.

4. There is no general carve-out from the SCM Agreement for agricultural products.

   However, the Agreement on Agriculture provides for a number of specific rules regarding subsidies on agricultural products which override certain specific provisions of the SCM Agreement.

   For example, during a nine-year implementation period, from 1995 through the end of 2003, domestic support measures covered by the "green box" of the Agriculture Agreement were, subject to certain conditions, non-actionable for purposes of countervailing duties as well as on a multilateral basis. During the same period, domestic support measures and export subsidies that conformed fully to a Member's reduction commitments under the Agriculture Agreement, or were exempt from such commitments, were exempt from multilateral challenge under the SCM Agreement.

   Other than the "green box" subsidies, however, subsidized agricultural products remained potentially countervailable during the implementation period.

   Since the expiry of the implementation period, agricultural subsidies are subject to the SCM Agreement (although with some modulation in some cases) and are countervailable.

   In addition, agricultural subsidies are notifiable under the SCM Agreement (as well as under the Agreement on Agriculture).

5. When it first entered into force, the SCM Agreement subdivided the subsidies that it covers (i.e., specific subsidies) into three categories: Prohibited (red light); actionable (amber light); and non-actionable

(green light). The non-actionable category was in effect for a period of five years, through the end of 1999, at which point it lapsed. The SCM Committee could have renewed the non-actionable subsidy provisions for a further period, with or without modifications, if it had been able to reach a consensus to do so before the end of 1999. No such consensus was reached, however. Thus, as of 1 January 2000, the previously non-actionable subsidies reverted to the actionable category, leaving the SCM Agreement with two covered categories of subsidies: prohibited and actionable.

6. A WTO Member that believes its interests are being harmed by another Member's subsidies has two possible options under the Agreement, depending on what kind(s) of harm it is experiencing, in which market(s):

   - a countervailing duty investigation; or
   - a multilateral dispute settlement challenge.

   If the Member believes that a domestic industry in its territory is suffering material injury as a result of subsidized imports, it may initiate a countervailing duty investigation, or seek WTO dispute settlement, as to subsidization, injury and causation. While countervailing measures are a unilateral instrument, the Member may apply them only after an investigation and a determination that the substantive criteria set forth in the SCM Agreement - the existence of subsidized imports, injury to the domestic industry, and a causal link between the two - are satisfied. A dispute settlement panel confronted with a claim of "injury" would have to conduct an identical analysis.

   If, however, the harm is being felt by the Member's exporters, either in the subsidizing Member's market or in a third country market, then the only available option is WTO dispute settlement, to consider whether the subsidies are causing serious prejudice or nullification or impairments of benefits to the complaining Member. Should the panel (and/or the Appellate Body) uphold the allegations of subsidization and adverse effects, the subsidizing Member would have to withdraw the subsidy or remove its adverse effects.

7. To have the legal basis to apply a countervailing measure on imports of a given product from a given country, a Member must determine that the imports are subsidized, that the domestic industry of the importing Member that produces the product that is "like" the imported product is injured, and that there is a causal link between the subsidized imports and the injury.

8. No. The importing Member can countervail only that portion of the subsidy amount that can reasonably be attributed to the investigated imported product. Because the company produces 20 products, and the subsidy is for its overall operations (not any particular product or subset of products), notionally the subsidy must be apportioned over all of those products (i.e., over the company's entire operations) on some sort of proportional basis reflective of the actual performance of the company. Then only that portion that has been apportioned to the investigated product could be considered a subsidy to that product.

9. Yes. The Agreement establishes different obligations for developing Members at different levels of development, in respect of the two kinds of prohibited subsidies.

   <u>Export subsidies:</u>

   In respect of export subsidies, the SCM Agreement accords differentiated treatment to three categories of developing Members:

   (i) least-developed country Members ("LDCs") (Annex VII(a) of the SCM Agreement) - exempt from the prohibition on export subsidies so long as they remain classified as LDC by the United Nations,

   (ii) certain Members listed in Annex VII(b) of the Agreement - exempt from the prohibition on export subsidies until their GNP per capita reaches USD 1,000 in constant 1990 dollars for three

consecutive years. (The constant dollar clause was introduced via Ministerial Decision at Doha in 2001); and

(iii) All other developing Members - were exempt from the prohibition on export subsidies for eight years following the entry into force of the SCM Agreement. Pursuant to an extension clause, some of these Members have obtained extensions of time for the phase -out of their export subsidies. The last of these phase-out periods will terminate at the end of 2015.

Import substitution subsidies:

LDC Members had eight years from the date of entry into force of the SCM Agreement (through the end of 2002) to eliminate their subsidies contingent on the use of domestic over imported goods. All other developing Members had five years (through the end of 1999).

There was no extension clause for these transition periods, and developing Members (as all other Members) have no further right to use such subsidies.

10. No. Subsidies contingent upon export performance are prohibited by the Agreement because they are designed (and presumed) to distort trade and thus harm the interests of other Members. These subsidies thus remain fully actionable (both subject to multilateral challenge in respect of their adverse effects, and countervailable) even for those developing Members that continue to have the right to provide them.

Videos

E-Learning short videos - Article 27 of the SCM Agreement - http://etraining.wto.org/admin/files/Trade_Course/SCM_art.27.mov

E-Learning short videos - Benchmarks for certain kinds of financial contribution - http://etraining.wto.org/admin/files/Trade_Course/SCM_benchmarks for certain kinds of financial contribution.mp4

E-Learning short videos - Benefit - http://etraining.wto.org/admin/files/Trade_Course/SCM_benefit.mp4

E-Learning short videos - Entrustment or direction http://etraining.wto.org/admin/files/Trade_Course/SCM_entrustment or direction.mov

E-Learning short videos - Export subsidies - http://etraining.wto.org/admin/files/Trade_Course/SCM_export subsidies.mp4

E-Learning short videos - Financial contribution - http://etraining.wto.org/admin/files/Trade_Course/SCM_financial contribution.mov

E-Learning short videos - Public body - http://etraining.wto.org/admin/files/Trade_Course/SCM_public body.mov

Other videos - http://www.youtube.com/user/WTO