

SUBSIDY DISCIPLINES

AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

SEMINAR ON WTO ACCESSIONS RULES

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Why do countries use subsidies?

- ❖ Governments use subsidies for a number of reasons such as...
 - Overcome market failures
 - Subsidies as instruments of economic and social policy
 - ✓ Even out regional economic disparities
 - ✓ Encourage certain sectors/technologies
 - ✓ etc.



Why does the WTO have an interest?

- ❖ Does the ASCM prohibit all subsidies?
 - Most forms of subsidies are allowed, but subject to disciplines
 - Only two kinds of subsidies are prohibited
- ❖ Why does the WTO regulate the use of subsidies?
 - They can distort international markets



WTO Agreements Prescribing Rules on Subsidies

- ❖ GATT 1994
- ❖ Agreement on Subsidies and Countervailing Measures (ASCM)
- ❖ Agreement on Agriculture



What does the ASCM do?

- ❖ Any distinctions such as industrial vs other types of subsidies?
- ❖ Two functions:
 - **Disciplines** the use of subsidies by WTO Members
 - **Regulates** the actions against the effects of subsidies
 - ✓ Multilateral
 - ✓ Unilateral - Countervailing measures



What does the ASCM do?

- ❖ Applies to **all WTO Members**
- ❖ Contains special provisions **in favour of developing Members**
- ❖ Establishes **detailed disciplines** on prohibited and non-prohibited subsidies
- ❖ Contains **detailed provisions** on types of subsidies, adverse effects of subsidies, unilateral use of CV measures, multilateral DS procedures, etc.



ASCM: Two Agreements in One

❖ Two Tracks

Multilateral Track

Establishment of a WTO DS panel, possible appeal, to determine:
(1) whether a measure is a prohibited subsidy; or
(2) whether a measure is a specific (actionable) subsidy causing adverse effects to the complaining Member.

Adoption of Panel/Appellate Body report by DSB

If DS ruling is favourable to the complaining Member:
- Prohibited subsidy - must be withdrawn by subsidizing Member.
- Actionable subsidy - must be withdrawn, or adverse effects removed, by subsidizing Member.

National (Unilateral) Track

Importing Member conducts investigation

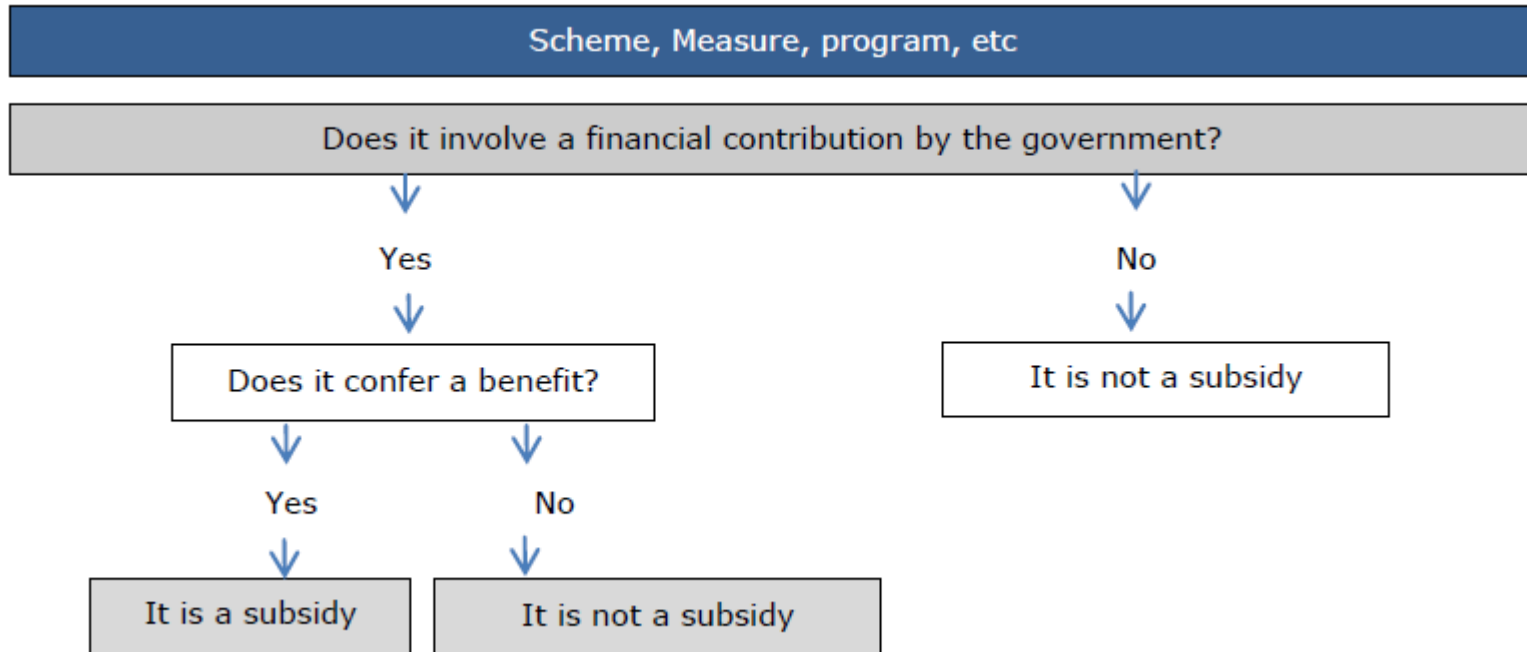
Determinations as to:
(1) Subsidization of investigated imports
(2) Injury to domestic industry producing like product
(3) Casual link

If affirmative determinations, importing Member can apply countervailing measure.

Investigation and/or determinations and/or measures can be challenged via WTO dispute settlement.

Coverage of the ASCM

❖ What is a subsidy?



Subsidy definition in the ASCM: Article 1

- ✓ A financial contribution
- ✓ By a government or any public body
- ✓ That confers a benefit
- ✓ Only those that are specific are covered by the ASCM



Financial Contribution: Art.1.1(a)(1)

- Direct transfer of funds, e.g.
 - Grants
 - Loans
 - Equity infusions
- Potential direct transfer of funds, e.g.
 - Loan guarantees
- Foregone or uncollected Government revenue, e.g.
 - Tax credits
 - Tax/duty exemptions



Financial Contribution...cont'd

- Provision of goods or services **other than general infrastructure**
- Purchase of goods
- Government payment into a funding mechanism
- Income or price support



Government or Public Body

- Government or public body makes financial contribution OR
- Entrusts or directs a private body to make financial contribution
- National-level governments/public bodies vs sub-national levels of government/public bodies

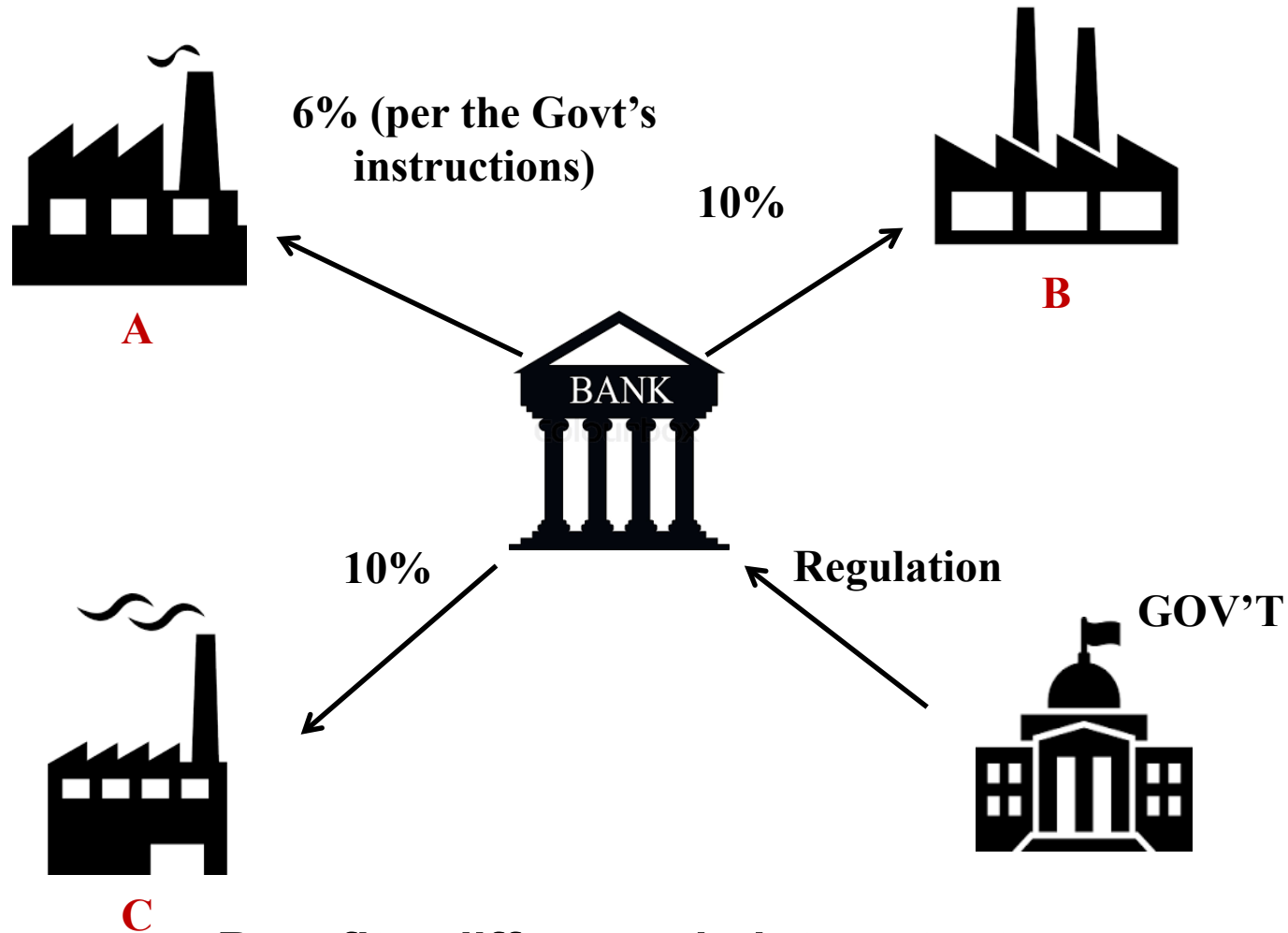


Benefit

- ❖ Advantage to recipient
- ❖ Compared to obtaining same financial contribution in market place
- ❖ Guidelines: Article 14 of the ASCM
 - Equity infusions by the government - the market-based comparison is with the "usual investment practice of private investors";
 - Government loans - the market-based comparison is with a comparable commercial loan that the borrower could actually obtain on the market;
 - 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;
 - Government provision of goods or services, or government purchase of goods.



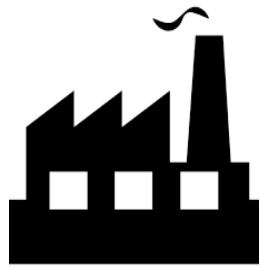
Benefit – Example: “Loan”



Benefit = difference in interest rates



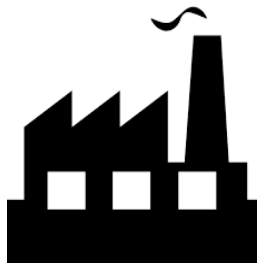
Benefit – Example: “Provision of goods”



Cars
10,000
USD/unit



PRIVATE MOTORS
Co.



Cars
8,000
USD/unit



GOV'T OWNED
MOTORS Co.

Benefit = 2000 USD/unit



Benefit – Example: “Purchase of goods”



SITUATION A
(price to private
company)

**100
USD/Unit**



PRIVATE PC Co.



SITUATION B
(price to Gov't)

120 USD/Unit



PRIVATE PC Co.

Benefit = 20 USD/Unit



Specificity

- **Limitation of access** to a subsidy to “certain enterprises”
- A subsidy is not subject to the ASCM unless it is specific
- Principle: Distorted resource allocation
 - Enterprise specific
 - Industry specific
 - Regional specificity
 - Prohibited subsidies deemed to be specific



Specificity...cont'd

- ASCM covers both *de jure* and *de facto* specific subsidies
- *De jure* specificity: access to subsidies is *explicitly* limited, in the law or by the granting authority, to certain enterprises.
- *De facto* specificity: access to subsidies is limited *in fact*



Specificity...cont'd

- Specificity can still be established if the facts demonstrate that **in practice** the subsidy is limited to only certain of the nominally eligible recipients.
 - 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.



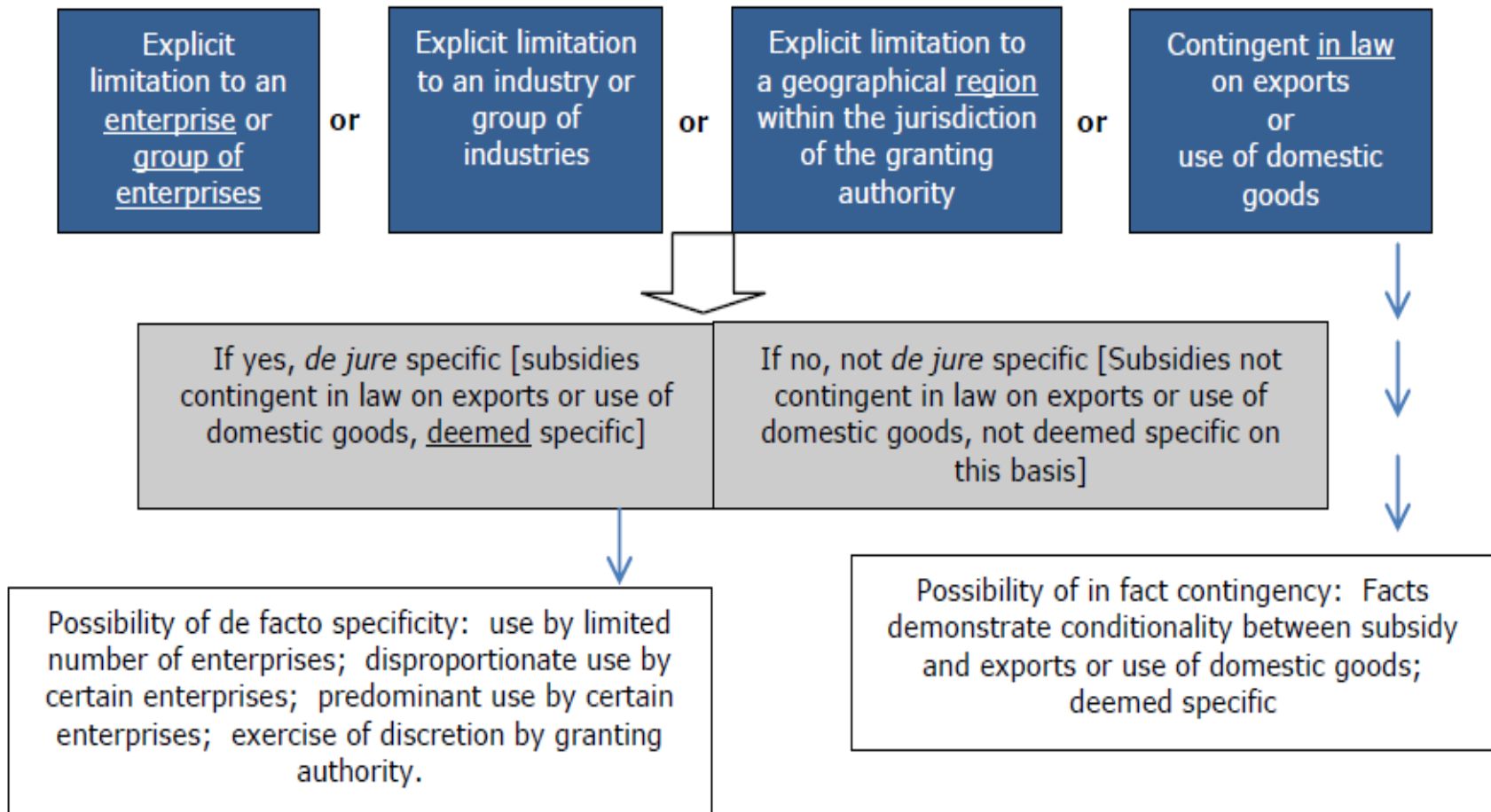
Specificity...cont'd

- Specificity cannot be found if eligibility for the subsidy is based on **objective criteria** ;
 - which are set forth explicitly in law, regulation or other official document and therefore verifiable;
 - those criteria are strictly adhered to and are applied in an automatic manner
- Objective criteria: neutral, that do not favour certain enterprises over others, and that are economic in nature and horizontal in application.



Specificity...cont'd

➤ How specificity works



Implications of Specificity

➤ For Members as providers of subsidies:

- Specific subsidies are subject to the rules/disciplines under Articles 4 and 7 SCM Agreement, in case of prohibited and actionable subsidies, respectively (**under the MULTILATERAL TRACK**); and can be countervailed (Part V) (**under the NATIONAL TRACK**)
- Must notify specific subsidies to the SCM Committee

➤ For Members affected by others' subsidies:

- Can challenge (**MULTILATERAL TRACK**) or countervail (**NATIONAL TRACK**) other Members' specific subsidies



CATEGORIES OF SUBSIDIES UNDER THE SCM AGREEMENT: PROHIBITED SUBSIDIES



Prohibited Subsidies

- Export subsidies
 - Subsidies contingent, in law (*de jure*) or in fact (*de facto*), upon export performance
 - **Annex I** to the ASCM
 - An illustrative **NON-exhaustive list** of export subsidies.
 - Measures not listed?
 - Check whether they meet the definitions of "subsidy" and export contingency.



Prohibited Subsidies...cont'd

- Import substitution subsidies (domestic content subsidies)
 - Subsidies which are "contingent" on the use of domestic over imported goods.
 - Contingency can be one among several other factors, and it can be either *de jure* or *de facto*.



Exceptions for Prohibited Subsidies

- S&D provisions on export subsidies
 - Annex VII countries (Article 27) – LDCs and countries listed in Annex VII(b)
 - Prohibition not applicable
 - Graduation at US \$1,000 GNP per capita
- **No exception** for domestic content subsidies!



CATEGORIES OF SUBSIDIES UNDER THE SCM AGREEMENT: ACTIONABLE SUBSIDIES



Actionable Subsidies

- All other **specific** subsidies
 - Adverse effects through use of subsidies, i.e.:
 - Serious prejudice
 - Injury to a domestic industry
 - Nullification or impairment of benefits



Serious Prejudice (Articles 5 & 6)

- Adverse trade effects through serious prejudice to the interests of a Member. Four possible scenarios:
 - Displace / impede imports of like product into subsidizing country market (Article 6.3(a))
 - Displace / impede exports from third-country market (Article 6.3(b))
 - Significant price undercutting, price suppression, price depression, or lost sales of like product in the same market (Article 6.3(c))
 - Increased world market share for primary commodity (like product by definition) (Article 6.3(d))



Actionable Subsidies – Injury

- Material injury or threat of material injury to the domestic industry producing the product that is "like" the subsidized product
- Material retardation of the establishment of a domestic industry producing that product.



Actionable Subsidies – Nullification or Impairment of Benefits

- 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



Actionable Subsidies – Nullification or Impairment of Benefits: An example

- 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 because Country A, begins to subsidize its domestic purchasers of barley by an amount equal to the tariff reduction.
- Purchasers continue to buy the domestic barley; therefore Country B's benefits have been nullified or impaired by Country A's subsidy.



Non-Actionable Subsidies

- **EXPIRED** at the end of 1999!
- The covered subsidies (specific R&D subsidies, environmental subsidies and subsidies to disadvantaged regions) reverted to actionable status



“REMEDIES” under the ASCM

Multilateral

Establishment of WTO
Panel

Adoption of Panel/AB
Report

Prohibited Subsidy:
Withdraw

Actionable Subsidy:
*Withdraw subsidy or
remove effect*

National

Initiate anti-subsidy (CVD)
investigation

Existence of subsidy, injury,
causal link

Impose countervailing
measures to offset subsidy



Surveillance of the ASCM

- ❖ The operation of the ASCM is overseen by the Committee on Subsidies and Countervailing Measures which;
 - is composed of representatives of **all WTO Members**;
 - **reviews all notifications** submitted by Members; and
 - **provides a forum** where Members can discuss any issue related to the operation of the SCM Agreement.



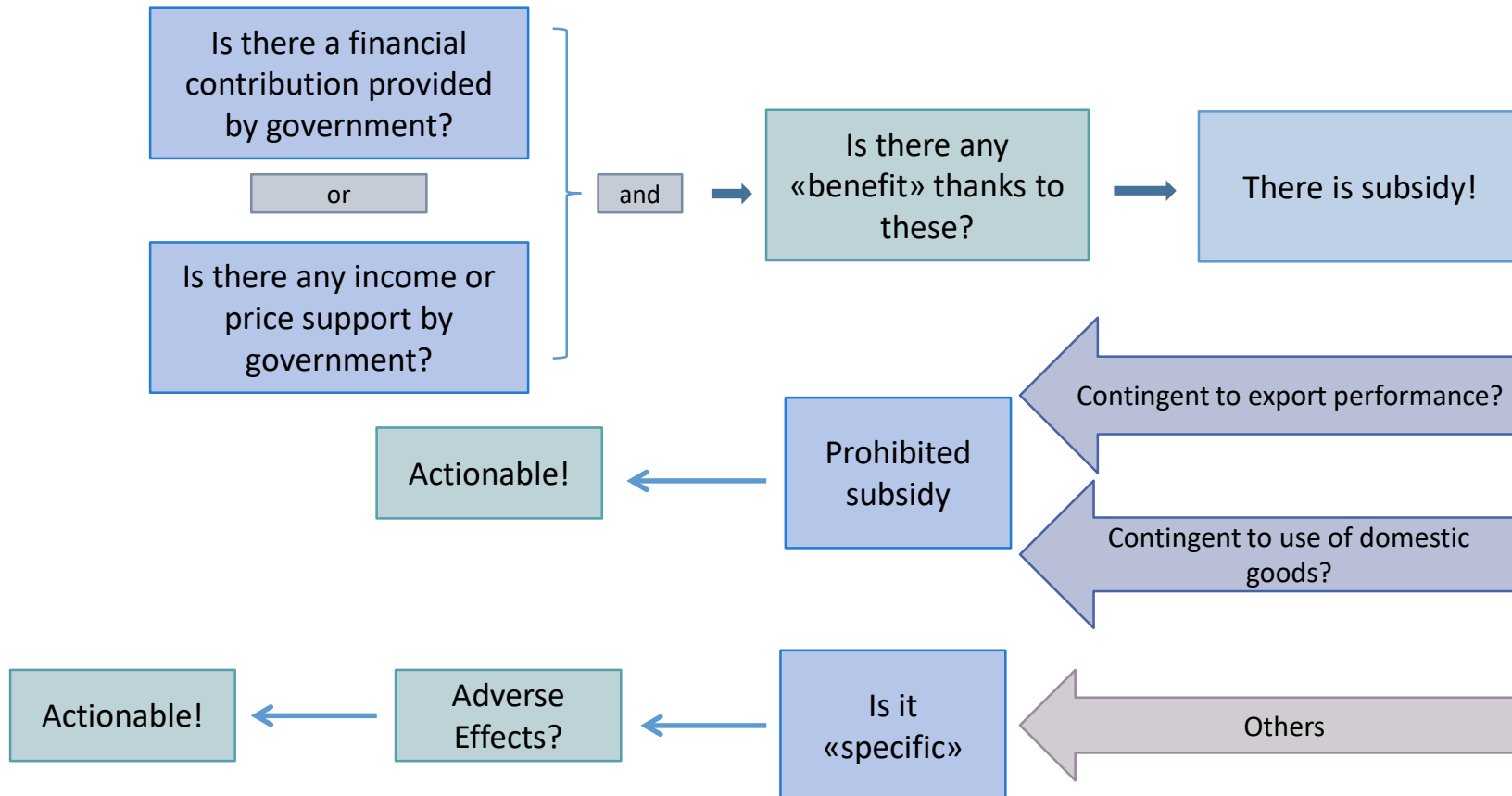
Discussion Question

- ❖ Are subsidies on agricultural products subject to the SCM Agreement?
 - There is no general carve-out from the SCM Agreement for agricultural products.
 - Agricultural subsidies are also subject to the ASCM and are countervailable.
 - In addition, agricultural subsidies are notifiable under the SCM Agreement (as well as under the Agreement on Agriculture)



Overview

- Subsidy: Legal Definition → ASCM Article 1



Free Zones and ASCM

❖ Benefits/advantages offered under the free zone regimes

- Fiscal incentives
 - Duty-deferral and duty-free treatment of exports
 - Exemptions from or reductions in inventory taxes and local taxes
 - Tax exemptions for corporate or personal income
 - Etc...
- Simplified customs procedures
- Infrastructure
- Working conditions/labour rules
- Exemption from trade measures
- Etc.



Free Zones and ASCM

- ❖ Not all advantages are within the ASCM definition – remember the definition of “financial contribution”:
 - Potential/direct transfer of funds
 - Forgone revenue
 - Provision of goods/services
 - Purchase of goods
 - Certain types of price or income support
- ❖ Two items are excluded from the definition
 - Support for general infrastructure
 - Exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption or remission of such duties or taxes



Free Zones and ASCM

- ❖ Some examples of specific subsidies that have been provided in free zones:
 - Exemption from import duties and charges
 - Total or partial exemption from direct taxes and social welfare charges
 - Exemptions from indirect taxes (e.g. sales taxes) and value-added taxes
 - Provision of goods and services to zone users at below market price
- ❖ Some advantages such as less onerous labour regulations or trade facilitating measures – not deemed to constitute financial contributions.



Free Zones and ASCM

❖ Risk of **prohibited subsidies**:

- requirements that zone users export a part of their production or that they use a prescribed level of domestically produced inputs in their operations

OR

- when the government imposes limitations on the extent to which goods in zones may be exported to the domestic market of the host countries



Free Zones and ASCM

- ❖ Even if there are no requirements to export, use domestically produced inputs or limitations on sales to the national customs territory the incentives provided in the zones may still qualify as actionable subsidies and are open to challenge by a WTO Member.
- ❖ Regardless of their classification as prohibited or actionable, any specific subsidy may also be subject to countervailing measures



Thank you for your attention...