

SUBSIDIES

Submission of the European Communities

The following communication, dated 20 April 2006, is being circulated at the request of the Delegation of the European Commission.

The submitting delegation has requested that this paper, which was submitted to the Rules Negotiating Group as an informal document (JOB(06)/118), also be circulated as a formal document.

In a recent submission¹ to the Group, the United States has proposed to expand the list of “prohibited” subsidies to cover additional subsidies having the potential to create significant trade distortions. This submission raises in fact two separate but equally challenging issues. The first issue is whether the expansion of the scope of the prohibition is an avenue that the Group wishes to pursue as a matter of general policy. The second issue concerns the identification of additional prohibited subsidies on the basis of objective criteria.

On the first issue, the EC sees merit in carefully revisiting the range of actions available to address the distorting effects of industrial subsidies. Clearly, a prohibition is an effective tool as it may help prevent the subsidy from being granted in the first place² though equally other forms of remedy available under ASCM could also be used. This deserves a thorough discussion in the Group with a view to assessing the implications on the overall structure of the *SCM Agreement* as well as the balance of rights and obligations among Members.

It is also important to note that State involvement is not *per se* indicative of subsidisation. Benefits cannot be presumed and the emphasis must be on the financial contribution being bestowed at below the relevant benchmark. Furthermore, there are a number of remedies available besides prohibition to address subsidies. And those remedies should also be examined to see whether they would not be appropriate for the trade distortion concerned. In short, one needs to clearly distinguish between two issues, i.e. the nature (or form) of the subsidy and its effects on trade when it comes to the remedy. In the EC’ view, it is the latter that should be decisive.

In this debate, the EC recalls its invitation to developing countries to identify possible constructive remedies instead of the normal measures that are currently imposed when injurious subsidisation is found. The EC takes this aspect of the negotiations very seriously and work on this should start as quickly as possible so that the needs of developing countries can be duly taken into account in the final outcome.

¹ TN/RL/GEN/94.

² This is the system that the EC has been implementing internally for State aid across the board. The EC would be pleased to share its experience with the Group

Discrimination in favour of domestic industries

The EC has long been concerned with the multiplication of government practices which favour domestic industries and which make available to domestic users some important inputs at a price substantially lower than the international market price. Such practice confers an evident benefit to the domestic users as compared to their foreign competitors who have to purchase their supplies at the (higher) international price.

In the EC's experience, the current *ASCM* discipline does not permit these practices to be tackled effectively. In view of the intrusive nature of such practices and the distortions they create, the EC considers that the difficulties in tackling such practices should be solved. To that effect, a possible solution would be to introduce a specific prohibition. However, other remedies could also be envisaged in certain circumstances.

The EC has also observed that other practices can also unfairly favour domestic operators as compared to their international counterparts. These actions impact on the availability of raw materials to the disadvantage of operators outside the country taking such actions. Specific remedies should be envisaged to deal with this type of situation.

In the same vein, it would be worthwhile considering the expansion of the coverage of Article 3.1(b) *ASCM* to align it to the national treatment provisions of GATT Article III, in order to prevent governments taking measures to favour the use of domestic inputs over imported ones. At the moment, Article 3.1(b) *ASCM* appears to require a demonstration of an absolute obligation to use domestic over imported goods, not just an encouragement or incentive to do so. This change would make it easier, for instance, to catch a local content requirement expressed in percentage of value-added, which may escape the current Article 3.1(b) provision.

Below cost finance

Harmful subsidisation often results where finance is available to economic operators at rates which do not cover the full cost of such finance. Such practices may be particularly difficult to address under the current *ASCM* rules for various reasons. In order to address this type of situation, one possible solution would be the introduction of specific language in the *ASCM* to the effect that the granting of loans below costs (or another suitable benchmark) could be adequately tackled if such practice is found to be generalised and systematic. Clearly, the new text would not cover isolated instances of lending below costs (or other relevant benchmark). Rather, it would be targeted solely at situations where the practice is generalised and systematic thanks to widespread State interference.

It is in the light of the above considerations that the EC is submitting the following textual proposal:

Annex – proposed changes to Article 3 of the *SCM* Agreement

3.1 Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

- (a) NO CHANGE
- (b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods **or subsidies inconsistent with Article III of the GATT 1994**
- (c) **the provision, by virtue of government action, of goods to domestic production on terms and conditions more favourable than those generally available for such goods when destined for export;**
- (d) **the provision, by virtue of government action, of finance to a wide range of industries on terms and conditions inadequate to cover the long term operating costs and losses of such finance where this benefits exported goods.**

3.2 A Member shall neither grant nor maintain subsidies referred to in paragraph 1.
