DRAFT REPORT ON THE OPERATION OF THE PROVISIONS OF ARTICLE XVI

I. INTRODUCTION

1. The terms of reference of the Panel on Subsidies state that the Panel is to undertake preparatory work for the review which the CONTRACTING PARTIES will conduct on the operation of the provisions of Article XVI and in particular:

(a) to examine the range and extent of subsidies maintained by contracting parties, in the light of the notifications submitted by them to the contracting parties, and of any other relevant information;

(b) to discuss with the notifying contracting parties any point requiring clarification and any other comment or suggestion put forward by other contracting parties to the Panel concerning the documentation received;

(c) to make practical suggestions to the CONTRACTING PARTIES with a view to improving the procedure for notifications; and

(d) to assemble materials for the draft report on the operation of the provisions of both sections of Article XVI.

In previous meetings the Panel has examined the range and extent of subsidies maintained by contracting parties, has discussed with the notifying contracting parties any points concerning the documentation received and has made suggestions with a view to improving the procedure for notifications. (See previous reports of the Panel on Subsidies, L/970 and L/1160 and Revised Questionnaire, L/1315.) The Panel therefore has concentrated, during its meetings in February and April 1961, on the assembling of material for a draft report on the operation of the provisions of both sections of Article XVI, as provided for in point (d) of its terms of reference.

2. The Panel has had at its disposal a good deal of information in the form of notifications of contracting parties, and with this information as background material, the Panel examined at its February and April meetings how the various
provisions of Article XVI have operated in practice. The Panel expresses the hope that the results of this examination, supplemented by the statistical survey and descriptive analysis prepared at the Panel's request by the secretariat, will assist in the review which the CONTRACTING PARTIES will conduct on the operation of Article XVI.

II. The rôle and effects of subsidies in international trade. (To be expanded after the Panel has had an opportunity to review the secretariat's statistical survey and descriptive analysis.)

3. Considering the rôle and effects of subsidies, the Panel had in mind whether subsidies were becoming more widespread and whether the effect of subsidies on international trade were comparable to tariffs, quantitative restrictions, etc.

4. In the early post-war years, of the barriers confronting international trade, tariffs and quantitative restrictions overshadowed most others, including subsidies. The effects of these barriers on trade, particularly quantitative restrictions, were at that time so restrictive that there was little attention directed towards subsidies as an obstacle to trade. At the present time, however, there is an increasing realization of the importance of subsidies as a commercial policy measure.

5. The Panel recognizes that there are cases where subsidies might have an advantageous effect, such as when there are abnormal increases in prices; subsidies then have the effect of permitting larger supplies to be placed upon the market, thus influencing the price. Similarly, it is recognized that subsidies do not have a damaging effect on international trade when they are effectively offset by measures such as acreage or production limitations and by measures designed to encourage consumption. However, the Panel feels that in many cases subsidies do have an adverse effect on international trade.

6. It could be said from perusal of the notifications that the majority of subsidies are subsidies affecting production of primary products. These measures are widespread and have become a common technique of income and price support. While it is the stated purpose of most subsidies to serve as a means
of income and price support, the result seems often to lead to increased production with a consequential effect on imports and exports. The Panel felt that a comprehensive statistical and descriptive survey, principally on a global basis and based on the material contained in the notifications, of the rôle and scope of subsidies in international trade in important primary and non-primary products, would be of assistance in the review of Article XVI. The Panel, therefore, requested the secretariat to undertake such surveys.

III. The use being made of Article XVI

7. The Panel discussed the various possibilities for consultations on subsidies and reviewed the consultations which had taken place between Governments:

(a) An agreement was reached in 1950 between the Governments of Australia and Chile regarding an Australian import subsidy on ammonium sulphate after a GATT working party had concluded that the Australian measure should be considered as relating to a benefit accruing to Chile under the General Agreement, and that it was therefore subject to the provisions of Article XXIII.

(b) An item concerning a United States export subsidy on oranges was placed on the agenda during the tenth session of the CONTRACTING PARTIES in 1955, but was later withdrawn in view of bilateral talks which had taken place between the Government of the United States and the Governments of Italy and the Union of South Africa. As a result of these talks the United States export payment on oranges was reduced from 75 United States cents to 50 United States cents per box.

(c) In 1956 the Government of Denmark gave notice (L/586) that it proposed to consult with the United States Government under the provisions of Article XVI regarding a United States export subsidy on poultry. Further information on this case was not transmitted to the CONTRACTING PARTIES;
(d) In 1957 the Government of Denmark, supported by the Governments of the Netherlands, Belgium, the Federal Republic of Germany and Sweden, complained that the export of eggs from the United Kingdom, the production of which enjoyed Government support by way of deficiency payments, had serious consequences on Danish exports. The GATT Intersessional Committee which had heard the complaint recommended that discussion should take place pursuant to Article XVI but decided to appoint a panel to examine this complaint if at any time it was reported to the Executive Secretary that the discussions had not led to a satisfactory solution. The discussions which followed, however, were successfully concluded and the United Kingdom authorities took measures to prevent exports of subsidized eggs from the United Kingdom to traditional Danish and Netherland's markets.

(e) In 1958 the Government of Australia complained that as a result of subsidies being granted by the French Government on exports of wheat and wheat flour, inconsistently with the provisions of Article XVI, French exports had displaced Australian trade in these products in its traditional wheat flour markets in Ceylon, Indonesia and Malaya, and had thus impaired the benefits which accrued to Australia under the General Agreement. The Panel for Conciliation (see document L/924) examined the complaint and decided to suspend consideration pending the outcome of bilateral discussions. However, bilateral discussions led to no satisfactory outcome and the Panel was reconvened. The Panel agreed on a text of a recommendation which, in its opinion, would assist the two Governments in arriving at a satisfactory solution. As a result of subsequent discussions between the two Governments, the French Government assured Australia that its flour export trade to traditional markets in South East Asia would not be materially affected by French competition during the current French export season.
8. The Panel notes that although all of the consultations referred to above involved subsidization measures, not all of the consultations had taken place under Article XVI; in at least one case (subsidized exports of the United States oranges), it is not clear under which Article consultations had been initiated. Consultations involving subsidization measures can be initiated either under Articles XVI and XXII on the one hand or under Article XXIII on the other. Consultations can be initiated under Article XVI if any subsidy operated either directly or indirectly to cause or threaten "serious prejudice" to the interest of any other contracting party. The additional provisions of Article XVI relating to export subsidies state that any subsidy on the export of primary products shall not be applied in a manner which results in a country having more than an "equitable share" of world export trade. There appears to be no evidence that the above-mentioned requirements for consultations under Article XVI constitute obstacles to the use of the consultation procedures of Article XVI. Indeed, there appears to be no evidence of difficulty of establishing on a case-by-case basis whether a country was suffering "serious prejudice" or was getting more than an "equitable share".

9. In addition to consultations under Article XVI, consultations may be initiated under Article XXIII if any contracting party should consider that any benefit accruing to it under the Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as a result of any situation, including the application of any measure, whether or not it conflicts with the provisions of this Agreement. If no satisfactory adjustment is effected between the contracting parties concerned within a reasonable time, it is possible to seek corrective action under Section 2 of Article XXIII.

10. The Panel noted that, unlike consultations under Article XXIII, consultations could be initiated under Article XVI without the necessity of prior action by the CONTRACTING PARTIES and in this regard referred to the Analytical Index of the General Agreement where it is stated that "consultation shall proceed upon the request of a contracting party when it considers that prejudice is caused or threatened and would not require a prior international determination".
11. The Panel also noted that consultations under Article XVI could take place whether or not a subsidy had been notified to the CONTRACTING PARTIES. In view of the hesitancy of some contracting parties to notify certain measures which they considered as borderline cases, the Panel points out that there is no obligation under paragraph 1 of Article XVI on a contracting party to consult on a particular measure by reason of the fact that the measure has been notified. Alternatively, failure to notify does not absolve countries from consultation under Article XVI. Consultations arise from injury and not from notification. The Panel expresses the hope that in cases of doubt contracting parties would decide to notify the CONTRACTING PARTIES of such measures; notification in many cases could have the effect of dispelling suspicion.

12. The Panel referred to the question of "serious prejudice". In the previous report of the Panel on Subsidies on 23 March 1960 (L/1160), the Panel tentatively concluded that, in the preparation of the draft report on the operation of the provisions of Article XVI it would wish also to have a look at the concept of serious prejudice. The Panel notes from the Analytical Index that:

"At the end of the Article the words 'it is determined that serious prejudice' were changed in the Charter text to 'a Member considers that serious prejudice' because 'it was thought that this change was consistent with similar changes in Chapter VI of the Charter and would expedite procedure'."

The Panel feels that it is therefore clear that a contracting party is not required to make out a prior case of serious prejudice in order to initiate a consultation under Article XVI. In this regard the Panel also referred to the report of the Review Working Party (BISD, Third Supplement, page 225) in which it is stated that some members of the Working Party preferred that "the language be re-drafted so as to make clear the intention of the present text, that is, that consultations can be initiated by a contracting party which considered that serious prejudice to its interests is being caused or threatened, without the necessity for prior action by the CONTRACTING PARTIES".
13. The Panel feels that the more complete information now available to contracting parties should enable countries to decide more easily whether "serious prejudice" to their interests is caused, and where bilateral consultations are unable to result in agreement on serious prejudice, the CONTRACTING PARTIES should be assisted in reaching a determination.

14. The Panel concluded that the limited number of consultations which had taken place under Article XVI should not be construed as evidence of the ineffectiveness of the consultation procedures of Article XVI. Indeed, where consultations had taken place they have generally proved successful. The more pressing obstacles of tariffs and quantitative restrictions, which until recently commanded most of the attention of contracting parties, undoubtedly had a bearing on the use which had been made of Article XVI. The Panel also considered that the present widespread use of subsidies possibly contributed in itself to the reluctance of governments to initiate consultations regarding subsidies, since they themselves employed similar measures.

IV. What constitutes a subsidy

15. The Panel points out that it is doubtful whether it is feasible or wise to secure an agreed interpretation of what constitutes a subsidy. On the one hand it would never be certain whether all cases of subsidies are in fact covered by a definition and, on the other hand, there is a danger that any definition would be too inclusive and, for example, possibly be in conflict with countervailing duty laws. In any event, the Panel felt that the lack of a precise definition of what constitutes a subsidy has not, in practice, interfered with the operation of Article XVI. The parties to previous consultations had managed to solve this problem in a practical way. The Panel considered that possibly the best alternative way to deal with specific cases as they arose, at which time it would be determined whether the subject of the complaint was in fact a subsidy.

16. The lack of any precise definition should not, in the Panel's view, have any bearing on whether or not certain measures should be notified. There is a legal obligation that all contracting parties should notify the CONTRACTING
PARTIES of the extent and nature of any subsidy which operates directly or indirectly to increase exports or to reduce imports. As a guide to the types of measures notifiable, the Panel referred to its report L/1160 of 23 March 1960.

17. The CONTRACTING PARTIES at the sixteenth session had approved a recommendation by the Panel for a revised questionnaire (L/1315). The Panel is generally satisfied with the replies thus far received in answer to this questionnaire, but expresses concern that less than one half of contracting parties have submitted notifications on the basis of the new questionnaire. The Panel draws the attention of the CONTRACTING PARTIES to the fact that the following countries had not, at the time of the Panel report, submitted notifications on the basis of the new questionnaire:

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<td>Brazil</td>
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<td>Burma</td>
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<td>Israel*</td>
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The Panel is aware from notifications submitted in reply to the previous questionnaire that certain of these countries maintain subsidies. In cases where these countries do not maintain subsidies covered by Article XVI, the Panel recommends that statements should be submitted to that effect.

18. The Panel discussed the question of the necessity of annually submitting notifications. The Panel recognized that for information such as the amounts of subsidies, which in most cases is subject to periodic change, there is a necessity for regular notifications. For other sections which are not subject to frequent change, such as the legal basis of subsidies, the Panel considers that unless there is a change to be reported it would be sufficient for contracting parties to inform the CONTRACTING PARTIES that there has been no change.

*Provisionally acceded or special relationship.
V. The position of the negotiability of subsidies

19. The Panel recalls that the Review Working Party on subsidies during the ninth session had agreed that "... there was nothing to prevent contracting parties, when they negotiated for the binding or reduction of tariffs, from negotiating on matters such as subsidies, which might affect the practical effects of tariff concessions, and from incorporating in the appropriate schedule annexed to the agreement, the results of such negotiations ..." (BISD, Third Supplement, page 225). The Panel notes that although certain countries had indicated that they did not expect to be able to negotiate concessions on non-tariff measures, the Rules and Procedures for the Tariff Conference (Section IIIb (ii) explicitly provide for the negotiability of a number of non-tariff measures, including subsidies. The Panel draws attention to the fact, however, that the negotiating rules make no reference to export subsidies, but only to subsidies which operate to "reduce imports".

20. Considering the provisions dealing with the impairment of tariff concessions, the Panel referred again to the Review Working Party report. This report states that "so far as domestic subsidies are concerned, it was agreed that a contracting party which has negotiated a concession under Article II may be assumed, for the purpose of Article XXIII, to have a reasonable expectation failing evidence to the contrary, that the value of the concession will not be nullified or impaired by the contracting party which granted the concession by the subsequent introduction or increase of a domestic subsidy on the product concerned". The Panel discussed at some length the meaning of "reasonable expectation" but concluded that no attempt should be made to define this phrase, but that it should be determined on a case-by-case basis.