On 9 July 1982 the Community submitted to the GATT a Memorandum on the US preliminary countervailing duty determinations on European steel exports. This document was discussed at the meeting of the GATT Committee on Subsidies and Countervailing Measures on 15 July 1982.

In the meantime the US Department of Commerce, on 24 August 1982, announced its final determinations, which were based on the same philosophy as the preliminary determinations although, due to certain refinements in methodology and to the use of more precise figures, the rates of subsidization found are, in general, lower than those in the preliminary determination.

The Community continues to view with concern the novel and unilateral interpretations of the GATT and the Subsidies Code which are contained in the US determination and has, therefore, up-dated its July submission to take account of the refinements in methodology in the final determination.

The Community urges that these issues be discussed at the next meeting of the Subsidies Committee.
A. General criteria for the determination of the existence of a subsidy

1. Charge on the public account

   a) EC argumentation

   Item (I) of the Illustrative List makes it clear that a charge on the public account is an indispensable prerequisite of any subsidy. This is borne out by the wording of the preceding items which repeatedly use such terms as "provision", "delivery", "remission", "exemption", "grant" by governments.

   b) US final determination

   "Item (I) (of the Illustrative List) does not limit the definition of subsidy to a charge on the public account, but rather makes clear that such a charge is included in the universe of subsidies which constitute on their face prohibited export subsidies. Items (c) and (d) of the List show that preferential treatment for exports, without regard to a charge on the public account, can also constitute a subsidy on its face ...."

   c) EC response

   The US argument is weak, in that items (c) and (d) of the List, which they cite, do involve a charge on the public account. The two items refer to the provision by the government of freight or products or services on terms more favourable than those generally available. The charge on the public account involved is the foregoing by the state in particular cases of the prices or tariffs which it is entitled to obtain for the product or freight in question.
The importance of item (I) is not that it limits the definition of a subsidy but rather that, as the last item in the list, it refers to "any other charge on the public account". The clear implication is that all the other subsidies also involve a charge on the public account.

The US position is extremely dangerous because, in its ultimate logic, it would assimilate a subsidy with any other government intervention in the economy, whether financial or merely regulatory e.g. price controls or pollution standards.

The fact that the benefit to the recipient is not the correct way to measure a subsidy can be demonstrated by looking at the problems involved in measuring the benefit.

Frequently, the recipients of grants do not have any possibility to make profitable use of the funds received because they are provided specifically to allow the company to restructure in a socially acceptable way.

It is clear therefore that the benefit of a grant to the recipient will vary according to the circumstances of the recipient at the time of receipt. There is therefore no simple or constant measure of the benefit and the difficulty of measuring it shows that, from a practical point of view as well as from a theoretical point of view, the correct measure of a subsidy can only be the amount of the financial contribution of the government.

It should be noted, also, that the US determination fails to carry the administration's thesis through to its logical conclusion. It is clear that even if the benefit to the recipient were the correct measure of a subsidy, there is no provision in GATT for taking account of a hypothetical benefit. If the subsidy is to be measured by benefit, then the actual benefit received by each company must be assessed on a case by case basis, taking account of the particular situation of each individual company.
2. **Benefit to recipient**
   
a) **US final determination**
   
   "Under the Act, the Department is required to determine whether respondents have received subsidies within the meaning of the Act. To do so, the Department seeks to determine whether or not respondents have received directly or indirectly an economic benefit..."

b) **EC response**

   EC agrees that not only must there be a charge on the public account, but that a benefit must thereby flow to an industry. While this benefit is necessary for a determination of the existence of a subsidy, it is not, however, the measure of the subsidy.

3. **Adverse effect on conditions of normal competition**

a) **EC argumentation**

   The subsidy must adversely affect the conditions of normal competition. In the absence of any such distortion, subsidies, other than export subsidies, are recognised as important instruments for the promotion of social and economic policy objectives against which no action is envisaged by the Code. It is fundamental therefore that the existence of such trade distortion is established, especially where signatories do not comply with the GATT principle that the amount of any countervailing duty should be less than the total amount of the subsidy if such lesser duty would be adequate to remove the injury. This is of particular importance in respect of programmes such as regional aids, R & D and coking coal programmes.

b) **US final determination**

   "... The argument of the EC flows against the logic of comparative advantage. Subsidies used to alter the comparative advantage of certain regions with respect to the production of a certain product or products are by definition distortive of trade and the allocation of resources, and, therefore, must affect normal competition, including competition with producers in the market of the importing country. There is no evidence that the governments of the countries in question, with regard
to most of the programs and benefits under consideration, specifically sought to avoid causing injury to the domestic industries of other Code signatories, or even considered possible adverse effects on trade, as required by Article 11:2 ..."

b) EC response

The EC argument that there must be distortion of competition and the US thesis that there must be a benefit to the recipient often lead to the same conclusion. It is through the benefit conferred that a subsidy may adversely affect the conditions of normal competition; in the absence of a benefit there can be no adverse effect on competition. The only question is whether every benefit necessarily results in distortion of trade.

As to the particular problem of regional aids, see item C. 5.

4. Sector specificity

a) US final determination

"Section 771(5) of the Act, in describing governmental benefits which should be viewed as domestic subsidies under the law, clearly limits such subsidies to those provided "to a specific enterprise or industry, or group of enterprises or industries." We have followed this statutory standard consistently, finding countervailable only the benefits from those programs which are applicable and available only to one company or industry, a limited group of companies or industries, or companies or industries located within a limited region.
or regions within a country. This standard for domestic subsidies is clearly distinguishable from that for export subsidies, which are countervailable regardless of their availability within the country of exportation. We view the word "specific" in the statutory definition as necessarily modifying both "enterprise or industry" and "group of enterprises or industries". If Congress had intended programs of general applicability to be countervailable, this language would be superfluous and different language easily could and would have been used. All governments operate programs of benefit to all industries, such as internal transportation facilities or generally applicable tax rules. We do not believe that the Congress intended us to counter-vail such programs...."

b) EC response

EC agrees. It must be recognized, however, that the requirement for sector specificity is additional to the other requirements such as benefit to recipient and adverse effect on competition. The specificity requirement, therefore, does not make regional aids countervailable where they simply compensate for dislocation costs.

5. Funding of aids

a) US final determination

"With respect to programs funded by the ECSC budget, we preliminarily determined that they do not confer countervailable benefits because for 1971-1980 (the last year for which complete data were available) their total amount did not exceed total levies collected from coal and steel producers within the ECSC member states...."

"... However, since 1978 member state contributions have constituted a portion of the ECSC budget. Upon consideration of this newly available information, for the years 1978-1981 we believe it is more reasonable to assume that programs funded by the ECSC budget are subsidized to the extent that the budget derives from member state contributions...."
b) **EC response**

EC agrees that aids funded from the levies collected from the beneficiaries of a particular government programme are not countervailable. The US position does, however, seem to be in direct contradiction of their argument that a countervailable subsidy does not presuppose a charge on the public account.

B. **Calculation of the amount of a subsidy and its allocation**

1. **Present value of subsidy and front-loading**

   a) **EC argumentation**

   Article VI GATT provides that a countervailing duty may not exceed the amount of the subsidy "determined to have been granted". The use of the word "granted" rather than "received" and the absence of any reference to "value" or "benefit" indicates clearly that the countervailable amount is the financial contribution of the government rather than the much more nebulous benefit to the recipient.

   b) **US position**

   "... It has been argued that $100 million today is much more valuable to a grant recipient than $10 million per year for the next 10 years, since the present value (the value in the initial year of receipt) of the series of payments is considerably less than the amount if initially given as a lump sum. We agree with this position and, as indicated in the preliminary determinations, have now changed our methodology of grant subsidy calculation to reflect this agreement. As long as the present value (in the year of grant receipt) of the amounts allocated over time does not exceed the face value of the grant, we are consistent with both our domestic law and international obligations in that the amount countervailed will not exceed the total net subsidy...."
"... Between the preliminary and final determinations we reviewed the comments and suggestions of various interested parties, principally contained in the pre- and post-hearing briefs. In addition, we sought the advice of an outside consultant with experience in the field of international investment banking.

On the basis of those discussions and that advice, we determine that the most appropriate discount rate for our purposes is the "risk-free" rate as indicated by the secondary market rate for long-term government debt (in the home country of the company under investigation ...."

"... In the past, we allocated the subsidy over only half the useful life in order to "front load" the countervailing duties, thereby complying with the legislative intent of the Act. However, so long as we allocate the subsidy in equal nominal increments over the entire useful life, it will still be effectively front-loaded in real terms (as long as a positive discount rate is used) since money tomorrow is less valuable than money today ...."

c) EC response

EC persists in disagreeing fundamentally with the US concept which has no basis in GATT. The fact that the discount rate now used has been changed does not alter that fundamental opposition.

The EC notes in addition that the US approach is inconsistent insofar as front loading is concerned.

If one were to accept the theory of present value it would logically result in a situation where the duty would have to increase in money terms each year. By allocating the amount of the subsidy, as calculated under the present value theory, in equal amounts over the life of the equipment, the duty is front-loaded instead of being back-loaded, which would be the logical result.
C. Specific programmes

1. Equity infusions
   a) US final determination

"... It is well settled that neither government equity ownership per se, nor any secondary benefit to the company reflecting the private market's reaction to government ownership, confers a subsidy. Government ownership confers a subsidy only when it is on terms inconsistent with commercial considerations. An equity subsidy potentially arises when the government makes equity infusions into a company which is sustaining deep or significant continuing losses and for which there does not appear to be any reasonable indication of a rapid recovery...."
"... If the government buys previously issued shares on a market or directly from shareholders rather than from the company, there is no subsidy to the company. This is true no matter what price the government pays, since any overpayment benefits only the prior shareholders and not the company;

If the government buys shares directly from the company (either a new issue or corporate treasury stock) and similar shares are traded in a market, a subsidy arises if the government pays more than the prevailing market price...."

"... It is more difficult to judge the possible subsidy effects of direct government infusions of equity where there is no market price for the shares (as where, for example, the government is already sole owner of the company). Government equity participation can be a legitimate commercial venture. Often, however, as in many of these steel cases, equity infusions follow massive or continuing losses and are part of national government programs to sustain or rationalize an industry which otherwise would not be competitive. We respect the government's characterization of its infusion as equity in a commercial venture. However, to the extent in any year that the government realizes a rate of return on its equity investment in a particular company which is less than the average rate of return on equity investment for the country as a whole (thus including returns on both successful and unsuccessful investments), its equity infusion is considered to confer a subsidy...."

b) EC response

EC welcomes the US acceptance of the fact that neither government ownership, per se, nor purchases of stock by a government on the open market at market price, constitute a subsidy.

It also notes with satisfaction that the US seem to accept that where there is evidence that the payment of a premium over the market price is warranted because of the asset value of the company or because of competing private bids for control, no subsidy would be determined to exist.
In cases of purchase by a government of stock for which there is no market price, the adoption, as a standard, of the average rate of return on investment in the exporting country is extremely arbitrary. Since the GATT criterion for the existence and measurement of a subsidy is the cost to the government, the transaction should be looked at in the long-term and the long-term (rather than year-by-year) return to the government should be compared with the cost to the government of borrowing the funds.

2. Loans and loan guarantees

a) US final determination

i) So-called creditworthy companies

"... The subsidy is computed by comparing what a company would pay a normal commercial lender in principal and interest in any given year with what the company actually pays on the preferential loan in that year. We determine what a company would pay a normal commercial lender by constructing a comparable commercial loan at the appropriate market rate (the benchmark) reflecting standard commercial terms. If the preferential loan is part of a broad national lending program, we use a national average commercial interest rate as our benchmark. If the loan program is not generally available — like most large loans to respondent steel companies — the benchmark used instead, where available, is the company's actual commercial credit experience (e.g., a contemporaneous loan to the company from a private commercial lender). If there were no similar loans, the national commercial loan rate is used as a substitute rate. Finally, where a national loan-based interest rate was not available, an average industrial bond rate was used as best evidence...."

"... After calculating the payment differential in each year of the loan, we then calculated the present value of this stream of benefits in the year the loan was made, using the risk-free rate (as described in the grants section of this appendix) as the discount rate. In other words, we determined the subsidy value of a preferential loan as if the benefits had been bestowed as a lump-sum
grant in the year the loan was given. This amount was then allocated evenly over the life of the loan to yield the annual subsidy amounts ....

"... A loan guarantee by the government constitutes a subsidy to the extent the guarantee assures more favorable loan terms than for an unguaranteed loan. The subsidy amount is quantified in the same manner as for a preferential loan...."

i) So-called uncreditworthy companies

"... Our use of the term uncreditworthy means simply that the company in question would not, in our view, have been able to obtain comparable loans in the absence of government intervention. Accordingly, in these situations neither national nor company-specific market interest rates provide an appropriate benchmark since, by definition, an uncreditworthy company could not receive loans on these or any terms without government intervention. Nor have we been able to find any reasonable and practical basis for selecting a risk premium to be added to a national interest rate in order to establish an appropriate interest benchmark for companies considered uncreditworthy. Therefore, we continue to treat loans to an uncreditworthy company as an equity infusion by or at the direction of the government. We believe this treatment is justified by the great risk, very junior status, and low probability of repayment of these loans absent government intervention or direction...."

b) EC response

The US decision is once again based on the potential benefit to the recipient rather than the cost to the government.

There is no basis in GATT for the distinction made in the US decision between creditworthy and uncreditworthy companies. Since the criterion for the existence of a subsidy is a charge on the public account, a distinction on the basis of creditworthiness, which is necessarily subjective, is irrelevant. The decisive question is whether the loan (including interest) was repaid. If it was and assuming that the rate of interest
was not less than the rate of interest paid by the government for the funds, no subsidy existed. If it was not repaid or if the rate of interest charged to the company was less than the rate at which the government borrowed the funds, then a subsidy existed, regardless of the creditworthiness of the company.

EC also disagrees with the use of the present value theory for the calculation of the amount of the subsidy because it is unreasonable to use this concept for loans since the subsidy which is being countered is on-going rather than being a lump-sum grant paid in advance and countered afterwards over a number of years.

3. Labour aids

a) US final determination

"... To be countervailable, a benefit program for workers must give preferential benefits to workers in a particular industry or in a particular targeted region. Whether the program preferentially benefits some workers as opposed to others is determined by looking at both program eligibility and participation. Even where provided to workers in specific industries, social welfare programs are countervailable only to the extent that they relieve the firm of costs it would ordinarily incur - for example, a government's assumption of a firm's normal obligation partially to fund worker pensions...."

b) EC response

EC agrees that, in order to be countervailable, labour aids must be specific and must relieve the company of a legal obligation.

4. Research and development aids

a) US final determination

"Grants and preferential loans awarded by a government to finance research that has broad application and yields results which are made publicly available do not confer subsidies...."
b) EC response

EC agrees that R & D aids are not countervailable if the results of the research are published.

5. Regional aids

a) US final determination

".... Subsidies used to alter the comparative advantage of certain regions with respect of the production of a certain product or products are by definition distortive of trade and the allocation of resources, and, therefore, must affect normal competition, including competition with producers in the market of the importing country ...."

b) EC response

No benefit is involved in government incentives to invest in dis­advantaged regions where these incentives are designed solely to compensate the dislocation costs of establishing industries in these regions. Regional aids are recognized in Article 11 of the Code as "important instruments for the promotion of social and economic policy objectives". Where they do not confer any benefit, they cannot, by definition, adversely affect the conditions of normal competition and therefore cannot possibly be considered as countervailable subsidies.