

**Committee on Subsidies
and Countervailing Measures**

**CHAIRMAN'S REPORT ON THE IMPLEMENTATION-RELATED
ISSUES REFERRED TO THE COMMITTEE AT THE REQUEST OF THE CHAIRMAN OF
THE GENERAL COUNCIL ON 2 AUGUST 2001 AND IN THE 15 DECEMBER 2000
DECISION OF THE GENERAL COUNCIL**

Mr. Chairman, I am presenting this report to the General Council on my own responsibility, as Chairman of the Committee on Subsidies and Countervailing Measures ("SCM Committee"), pursuant to your 2 August 2001 request that the Committee take up two new implementation issues, and report back to the General Council by 30 September 2001. The two new issues were (1) consideration of the implementation of Article 27 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") as it relates to particular issues concerning developing country Members with a small percentage share of exports in import markets and in global trade; and (2) review of the provisions of the Agreement on Subsidies and Countervailing Measures regarding countervailing duty investigations.

Mr. Chairman, you will recall that in the report that I submitted to the General Council on 31 July 2001 in respect of the three implementation-related issues referred to the Committee in the General Council's decision of 15 December 2000, I indicated *inter alia* that I believed that there was potential for a possible solution in respect of one issue – export competitiveness – with additional time and effort by the Committee. I therefore indicated that Members would have the opportunity in September to continue addressing this and the other two issues referred on 15 December.

The Committee has had a very active programme of meetings and consultations during September, in the course of which all relevant matters have been addressed. All Members have engaged seriously and constructively in this work, and I believe that we have made considerable progress in clarifying some of the many technical aspects involved, and in working toward identifying the bases of possible solutions on at least some of these issues. This said, there is much more work to be done before fully-elaborated proposals can be formulated.

In view of both the progress that we have made so far, and the amount of work that remains to be done, the Committee has agreed to keep working in the time remaining until the Ministerial Conference in Doha. The Committee has, moreover, taken note of the draft implementation decision in the text that you circulated on 27 September 2001 which, if adopted by the General Council, will instruct the Committee to continue to work on the countervailing duty investigation issue between now and Doha. With these considerations in mind, the Committee has agreed on a work plan of meetings and consultations that it would pursue between now and 26 October, in the event that the General Council decides to extend the Committee's mandate in respect of these issues.

Mr. Chairman, I would therefore recommend that the General Council extend the mandate of the Committee until 26 October.

During the time of that extension, in respect of issues concerning the implementation of SCM Article 27, the Committee would:

- Continue to work with a view to reaching a solution for developing country Members with a small percentage share of exports in import markets and in global trade, within the framework of Article 27.4 of the SCM Agreement for extensions of the transition period for export subsidies. In this connection, the Committee would seek to identify criteria for eligible countries and programmes, transparency elements, timeframes, and any other relevant elements and operational aspects.
- Continue to work with a view to reaching a solution on the export competitiveness issue. In this connection, work on a possible solution on the determination of export competitiveness would focus on elaboration of an approach based on moving averages to determine shares of world trade in a product. Work on the possibility to resume export subsidization following a loss of export competitiveness would continue on the basis of ideas previously advanced, including the "stop-the-clock" approach described in detail in my first report.

In respect of the review of countervailing duty investigation procedures, the Committee would continue to discuss the proposals received, and report to the General Council.

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Mr. Chairman, I would like to conclude this report by again expressing my gratitude to all Committee Members and the Secretariat for their very hard work. It would not have been possible to progress in our discussions if not for the flexibility shown by all Members in evaluating various ideas and possibilities for solutions to these important issues. The Committee is prepared to continue to work intensively in the weeks to come, and I remain optimistic that on that basis we may be able to produce some concrete suggestions for consideration at Doha. I look forward to the results of the General Council's deliberations in this respect.

Remo MORETTA
Chairman
Committee on Subsidies and Countervailing Measures

30 September 2001

Technical summary

1. Procedure

1. This is my second report in connection with the implementation-related issues referred to the Committee from the General Council. The first report (G/SCM/34, dated 31 July 2001) covered the Committee's discussions on the issues that had been referred to it from the General Council up to that point, namely the issues of export competitiveness (SCM Articles 27.5 and 27.6); and aggregate and generalised rates of remission of import duties, and the definition of "inputs consumed in the production process", taking into account the particular needs of developing countries.

2. At the 31 July 2001 informal meeting of the General Council, the General Council Chairman indicated his intention to request that the SCM Committee take up two more issues, and report back to the General Council by 30 September 2001. This request was conveyed to me in a letter dated 2 August 2001. The two issues were (i) a review of the provisions of the SCM Agreement regarding countervailing duty investigations; and (ii) the implementation of Article 27 of the SCM Agreement as it relates to particular issues concerning developing country Members with a small percentage share of exports in import markets and in global trade.

3. The Committee had agreed at its meeting of 27 July 2001 that any new referrals that it might receive from the General Council would be considered using the same basic procedures as had been followed for the referrals of December 2000. In this regard, specifically, the Committee agreed that Members wishing to raise particular issues under the new referrals should make brief written submissions, identifying the relevant provisions of the Agreement, outlining the problems or issues of concern, and suggesting any solutions. Such papers were to be submitted to the Secretariat by 27 August 2001. New proposals were received from El Salvador and Jamaica in respect of the issue of developing country Members with a small share of trade, and from India and Brazil in respect of countervailing duty investigation procedures. India and Brazil each submitted an additional document in response to a request for some categorisation of the issues that they raised. The Dominican Republic submitted a document, also on behalf of Bolivia, Ecuador, El Salvador, Guatemala and Honduras, containing a declaration adopted at the Fifth Latin American Conference on Free Zones, held recently in Panama.¹

4. The Committee met on 11, 18, and 28 September 2001 in informal session, and on 28 September 2001 in formal session, to discuss the substance of the two new referred issues, and to continue work on the referrals of December 2000. In between the meetings of the Committee, a series of informal consultations were also held. These discussions were based on the written proposals and papers submitted by delegations, as well as documents that I prepared, including non-papers summarising the discussions at the Committee meetings.

5. At its formal meeting of 28 September 2001, the Committee agreed that it would continue to work, on the assumption that its mandate would be extended. With this in mind, the following work plan was adopted: the Committee would meet in informal and/or formal session on 12 and 26 October 2001, and I would hold informal consultations on 4 and 9 October 2001, and other dates as appropriate, with a view to advancing discussion of the referrals on the basis of the elements outlined.

6. In the following sections, the main points raised in the discussions are summarised. In giving due consideration to the issues, these summaries should be read in conjunction with the papers exchanged by Members, the records of the Committee's meetings on these issues, and the other documents referred to herein.

¹ G/SCM/W/467.

2. Developing country Members with a small share of trade

7. In his request of 2 August 2001, the Chairman of the General Council indicated that an understanding had been reached to refer the following proposal to the SCM Committee:

"Members request the Committee on Subsidies and Countervailing Measures to consider the implementation of Article 27 of the Agreement on Subsidies and Countervailing Measures as it relates to particular issues concerning developing country Members with a small percentage share of exports in import markets and in global trade."

8. Pursuant to the procedures agreed by the Committee, El Salvador and Jamaica submitted proposals in respect of this issue.

(a) Proposal of El Salvador²

9. El Salvador's proposal targets "free zones", established for development and employment purposes and located outside its national customs territory, which provide exemptions from internal taxes, including taxes on profits, and import duties. Goods produced or processed in the zones are temporary importations, with internal taxes and import duties being paid on the goods exported from these zones in the countries into which the goods are re-exported upon production or processing. El Salvador proposes an interpretation under which such exemptions from internal taxes and import duties would not be considered export subsidies.

10. The following points were made in respect of El Salvador's proposal on this issue:

- Scope of proposal – Some Members sought details of the different incentives provided in free zones. In this regard, they raised the question of whether any action or interpretation would be necessary in respect of duty drawback or other incentives not contingent upon export performance.
- Basis of proposed exemption – On the other hand, some Members questioned the basis on which an exemption from taxes on profits derived from exportation could be deemed not to be an export subsidy.

(b) Proposal of Jamaica³

11. Jamaica proposes an exemption for certain developing country Members from the prohibition on export subsidies. Beneficiaries of this proposal would be defined according to their share of global merchandise trade. Further, where such a Member had no greater than a 3.25 per cent share of world trade in a particular product, the prohibition on export subsidies would not apply to that Member in respect of that product.

12. The following points were made in respect of Jamaica's proposal on this issue:

- Definition of eligible Members – Some Members questioned the appropriateness of the 0.05% threshold share of world trade proposed by Jamaica, which they considered to be arbitrary in the absence of any concrete justification for that level.
- Operation of exemption – A number of Members indicated an unwillingness to consider an indefinite exemption from the prohibition on export subsidies as proposed by Jamaica.

² G/SCM/W/461.

³ G/SCM/W/463.

They suggested as an alternative that they could consider finding a solution for developing country Members with a small share of trade within the framework of the mechanism in SCM Article 27.4 for extension of the transition period for developing country Members' export subsidies. Under this suggested approach, any Member seeking an extension of the transition period under Article 27.4 would have to present an application to the Committee. Such an application would need to be detailed and could identify, for instance, the type of programme, the main beneficiaries thereof, and the volume/scope or coverage of the subsidies involved. Extensions would be subject to annual monitoring, as foreseen in Article 27.4. To ensure certainty, quantifiable criteria would need to be established and those suggested by Jamaica were useful in this regard as a basis for further development or work. Any extensions would need to be time-limited and there would be no change to an extension once granted, subject to monitoring.

- Standstill – Several Members suggested that any extensions would be limited to existing programmes and that the levels/scope of benefits could not be increased.
- Jamaica indicated its willingness to continue to seek solutions on the basis of the elements outlined.

(c) Possible alternative framework

13. Following discussion of the two proposals on this issue, I suggested in a round of informal consultations that a solution might be possible combining elements from both El Salvador's and Jamaica's proposals, as well as elements suggested in the Committee's discussion. Under this approach, the question of the export subsidy prohibition as it applies to developing country Members with a small share of trade would be addressed through the framework of the extension mechanism in Article 27.4. In this context, extensions of the transition period for such Members would be limited to existing import duty and internal tax exemptions provided in the context of economic and social development programmes geared toward attracting investment, to be notified in the application for an extension.

14. For a measure to qualify, it would need to have been in existence as of a set date in the recent past. The scope and coverage of the notified measures, and of the intensity of subsidisation thereunder, could not be increased during the period of extension. Developing countries would be deemed to have a small share of world trade, and thus be eligible, if their share of world merchandise export trade was not greater than a set percentage. Further, an extension would be granted upon application to the Committee, to be made by 31 December 2001. Any extensions would be subject to annual review, and extensions would be continued on the condition that transparency and standstill requirements were met. The extension would be terminated in respect of any individual product in which the beneficiary reached at least a 3.25 per cent share of world trade. This framework would be without prejudice to Articles 27.5 and 27.6 or to any proposals related to them, and to any requests for extensions under Article 27.4 not made pursuant to this framework.

15. Following my consultations, the Committee agreed to pursue work in respect of the issue of developing country Members with a small trade share on the basis of the Article 27.4-based approach that I had outlined, with the details as to eligibility and operation to be negotiated by Members. This further work would be without prejudice to Members' final positions and to any other proposals.

16. Concerning the details of the approach outlined, the following are the main points that have been raised:

- Systemic concerns – Some Members have expressed concerns over the increasing categorisation of Members, including within the category of developing countries. Views were also expressed that this framework would weaken subsidy disciplines and, in

particular, would allow for continued export subsidization, which was a matter of serious concern to some.

- Eligibility for extensions – Several Members have suggested that additional elements – besides percentage share of world merchandise export trade – be considered as possible criteria for determining a Member's eligibility for an extension under this framework. Such criteria might include, *inter alia*, population, GDP/GNP (as a total or on a per capita basis), export subsidies as a percentage share of total exports, and/or other relevant factors. In this regard, the Secretariat has been requested to provide additional statistical information which may assist Members in determining the most relevant criteria to be applied. One Member has emphasised that the eligibility criteria must seek to identify countries that are vulnerable in the multilateral trading system. Suggestions were also made that the framework should involve an agreed list of criteria, or an agreed list of Members that meet an agreed list of criteria. Some Members have expressed a preference for a positive list of programmes, and some for identification of particular sectors. One Member suggested that a pragmatic approach be adopted, involving a combined country/programme perspective with respect to eligibility, which would provide a precise idea of the scope of this framework. Others have commented on the difficulties in defining a category of eligible countries. Concerns have also been expressed in respect of transparency with regard to eligibility criteria.
- Definition of "existing programmes" – Some Members have suggested, on the basis of the requirement in Article 27.4 not to increase the level of export subsidization, that only programmes in existence as of 1 January 1995 should be eligible for extensions. Another Member has suggested that only programmes in existence as of 31 July 2001 should be eligible for extensions. A third suggested cut-off date, which I put forward for consideration, was 1 September 2001.
- Notification of beneficiary programmes – Several Members have indicated that notification of the beneficiary programmes should be a necessary pre-condition of any extension. In this respect, it has been suggested that the format for notifications under Article 25 would be appropriate.
- Period of extension – Most Members have stated that the period of extension would need to be limited, with one Member specifically proposing that the period be three years.
- Continuation of extension – Some Members have suggested that the annual reviews be conducted on a pro forma basis, with extensions continued ex ante on the condition that standstill and transparency requirements are respected. One Member has indicated that this possibility would only be appropriate if the agreed period of extension is a short one, but that a long period of extension would require a phase-out or staging provision.
- Annex VII countries – The question of Annex VII countries was raised, with some pointing out that any countries that graduate out of Annex VII after 31 December 2001 would not be able to take advantage of this framework, and thus would be worse off than those who have already graduated as of that date. Accordingly, it was suggested that "late" graduates be considered eligible for an extension equal to the remaining time-period at the time of their graduation from Annex VII.
- Possibility of safeguard measures – One Member has suggested that importing developing country Members adversely affected by an extension granted to another Member under the proposed framework should be allowed the possibility of adopting safeguard measures in respect of their domestic industries. It was not clear whether such

safeguards would be applied within or outside of the context of the Safeguards Agreement.

3. Export competitiveness

17. As suggested in my 31 July report, the Committee continued its discussion of export competitiveness in the course of its September 2001 activities. As noted in that report, the proposal on this topic (G/SCM/W/431/Rev.1) contains two elements: (i) the proponents seek a change from 2 years to 5 years for the period over which export competitiveness is to be established under Article 27.6; and (ii) the proponents seek a mechanism to allow developing countries that have achieved export competitiveness in a product to resume export subsidization on that product if exports thereof fall below the export competitiveness threshold.

18. Concerning the **first element** of the proposal (i.e., on the establishment of export competitiveness), the following are the main points that have been raised during the September 2001 discussions:

- Suggestion of a moving average for determining export competitiveness – Concerning the proposal to change the period for establishing export competitiveness from two consecutive years as set forth in Article 27.6 to five consecutive years, some Members have noted that this proposal seeks to address the problem that the period of two consecutive years might not be a sufficient period of time to reflect stable conditions. It has been suggested that an alternative means of addressing this problem, which would not require an amendment to the Agreement, would be to calculate the shares of trade for each year in a two-consecutive-year period on the basis of two-, three-, or four-year moving averages. That is, the data for each year of the two-year period would consist of a multi-year average of the data for that year and some number of immediately preceding years. Such an approach would smooth abnormal fluctuations that might occur sporadically, and thus should help to prevent countries from crossing the 3.25 per cent threshold on the basis of transitory conditions, and then dropping back below that threshold once those conditions had passed.⁴ To ensure that no Member is made worse off under this approach than under an approach based on two consecutive individual years of data, the moving average would be applied only in cases where the trade shares in the product were at least 3.25 per cent during each of the two individual consecutive years in question. That is, if a country in two consecutive years had at least a 3.25 per cent share of trade in a product, then the moving-average calculation would be performed to determine whether, on that basis as well, the 3.25 per cent threshold had been reached in two consecutive years.
- Basis for further discussion – The proponents have indicated that their original proposal on export competitiveness was intended to address more than the question of volatility. That said, they have indicated that they would be willing to work on the basis of the moving-average idea as a possible means of addressing the first element of their proposal, without prejudice to the second element of their proposal (resumption of export subsidisation after a loss of export competitiveness). The Committee has agreed to pursue this element of the export competitiveness proposal on this basis, without prejudice to Members' final positions or to any other proposals.
- Trigger for/starting-point of the phase-out period – Some Members have expressed reservations over the pending suggestion that the phase-out period after reaching export competitiveness would only start as of the time that a determination was made that

⁴ Japan has submitted a useful simulation illustrating how the concept of moving averages would operate.

export competitiveness had been reached. In the view of these Members, the language of the Agreement is clear that the phase-out period begins when, on the basis of historical data, a country first reaches export competitiveness.

- Relationship of the first and second elements of the export competitiveness proposal – The proponents have indicated that the first and second elements of their proposal should continue to be discussed, and should be resolved, together. While all Members are willing to continue to work on both elements, some remain of the view that the two elements are mutually exclusive. In addition, certain delegations have recalled that any solution in respect of export competitiveness would be subject to their previously-expressed reservations concerning Annex VII.

19. Concerning the **second element** of the proposal (i. e., the possibility of allowing developing countries to resume export subsidisation once competitiveness was lost), the Committee has agreed that further work should continue on the basis of the elements currently under discussion, including in particular, the "stop-the-clock" idea:

- EC "stop-the-clock" proposal – Under the EC's proposed "stop-the-clock" approach⁵, if a developing country Member that had reached export competitiveness then lost it during the ensuing eight-year phase-out period, that phase-out period would be stopped until export competitiveness was reached again. At that point, the Member would have the remainder of its eight-year period to complete the phase-out of its export subsidies on that product. If, however, there were less than two years remaining of the eight-year period at the time that export competitiveness was lost, the Member would have two years to complete the phase-out of the export subsidies. Similarly, if export competitiveness were lost after the end of the eight-year phase-out period, under this approach the Member could re-introduce export subsidies on that product, and then would have two years to phase them out once export competitiveness was again reached. The proponents have indicated their willingness to use this approach as the basis for further discussion and elaboration in respect of the second element of their proposal.
- Possible duration of export subsidisation: Certain Members have expressed concern that under the stop-the-clock proposal there might be an endless loop of export subsidisation. This would be particularly so if a country were to fluctuate above and below the export competitiveness threshold even for extended periods, so long as those periods were less than the minimum periods for reaching and losing export competitiveness. Some Members have indicated that they could not support any resumption of export subsidisation after the original eight-year period had run its course.
- Level of subsidisation: Some Members have indicated that there should be no increase in the level of subsidisation during any period in which the clock was stopped.
- Transparency/Monitoring: Some Members have noted that a system such as the one outlined in the stop-the-clock paper would require detailed monitoring to function properly. The proponents have indicated a preparedness to establish a monitoring mechanism. However, the impact of such a mechanism, in view of the resource constraints of small delegations, would need to be assessed.

⁵ G/SCM/W/457.

4. Countervailing duty investigation procedures

20. In his request of 2 August 2001, the Chairman of the General Council indicated that Members were agreeable to the terms of the following referral to the Committee:

"That the Chairman of the General Council request the Committee on Subsidies and Countervailing Measures to review the provisions of the Agreement on Subsidies and Countervailing Measures regarding countervailing duty investigations, and to report to the General Council by 30 September."

21. Pursuant to the procedures agreed by the Committee, India and Brazil submitted proposals⁶ in respect of this issue. Following discussion of these proposals, both Members submitted further papers⁷.

22. The following **general points** have been made concerning the two proposals:

- **Relationship between proposals** – Some Members have raised the question of whether India's and Brazil's papers can be substantively rationalised in some way. Brazil has indicated that, to the extent possible, it is in favour of this proposition, but that difficulties might arise in such an exercise, due to different perspectives taken in the two proposals. India has indicated that, while it considers the two proposals complementary, there are sufficient differences in points of emphasis to warrant separate consideration of each proposal.
- **Nature of issues raised** – Some Members have also raised the question of a distinction between those issues which arise due to silence or ambiguity in the text of the Agreement and those which would require amendment of existing provisions of the Agreement. India has indicated that additional disciplines are required in respect of the following elements of its proposal: (i) deductions and adjustment on account of expenses which the exporter has to incur to obtain the alleged subsidy; (ii) review of countervailing duty on submission of positive information regarding procedural mistakes or manifest errors of apprehension and withdrawal of subsidy schemes considered to confer a benefit; and (iii) review of benefit conferred by subsidy schemes which have been subsequently terminated. The other elements of its proposal would require only clarification of the relevant provisions of the Agreement. Brazil has indicated that its proposals for the inclusion of additional guidelines to Article 14 and provisions related to sampling might be considered to require some sort of amendment to the Agreement, whereas the other points could probably be solved by means of interpretation of lacunae in the text of the Agreement.
- **Possibility to draw on elements in the Anti-Dumping Agreement** – With regard to its suggestion to introduce into the SCM Agreement rules on sampling and facts available such as those contained in the Anti-Dumping Agreement, Brazil has indicated that the anti-dumping rules might be a good starting point, but that some other elements might also be introduced.

5. Definition of "inputs consumed in the production process"

23. No further substantive issues have been raised in respect of this issue since my 31 July report.

⁶ The proposals can be found in documents G/SCM/W/462 and G/SCM/W/464.

⁷ G/SCM/W/465-466.

6. Aggregate and generalised rates of duty remission

24. No further substantive issues have been raised in respect of this issue since my 31 July report.⁸

⁸ A factual background note was submitted with no substantive discussion (G/SCM/W/460).