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DOMESTIC SUBSIDIES UNDER THE WTO AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES AND THEIR TREATMENT IN SECTION 771 OF THE TARIFF ACT OF 1930

CECIL CARL-ERICH KRAMER

University of Georgia School of Law

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ON SUBSIDIES AND COUNTERVAILING MEASURES
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SECTION 771 OF THE TARIFF ACT OF 1930

by

CECIL CARL-ERICH KRAMER

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Second Judicial State Examination, Stuttgart, Germany, 1998

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of The University of Georgia in Partial Fulfillment
of the
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ATHENS, GEORGIA
1998
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by

CECIL CARL-ERICH KRAMER

Approved:

[Signature]
Major Professor

Date
April 28, 1999

[Signature]
Chairman, Reading Committee

Date
May 13, 1999

Approved:

[Signature]
Graduate Dean

Date
May 31, 1999
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I. Introduction

The provision of subsidies by governments is a widespread practice. Recent years saw a steady rise in the provision of subsidies by OECD countries.\(^1\)

Subsidies in Billion US-Dollars\(^2\)

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<thead>
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<tbody>
<tr>
<td>OECD-Total</td>
<td>317.02</td>
<td>392.54</td>
<td>485.86</td>
</tr>
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<td>EC 15</td>
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<td>33.5</td>
<td>32.9</td>
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</table>

Governments provide subsidies for a variety of reasons and they are an important tool "to promote important

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\(^1\) The Organization for Economic Co-operation and Development (OECD) is comprised of industrialized countries, all of which are Members of the OECD Convention, which entered into force on September 30, 1961. See OECD, Annual Report 1997 (1998). The following countries are currently members of the OECD: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Italy, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States. The Commission of the European Communities takes part in the work of the OECD.
objectives of national policy."^3 Among those objectives are:

"(a) the elimination of industrial, economic and social disadvantages of specific regions,

(b) to facilitate the restructuring, under socially acceptable conditions, of certain sectors, especially where this has become necessary by reason of changes in trade and economic policies, including international agreements resulting in lower barriers to trade,

(c) generally to sustain employment and to encourage re-training and change in employment,

(d) to encourage research and development programmes, especially in the field of high-technology industries,

(e) the implementation of economic programmes and policies to promote the economic and social development of developing countries,

(f) redeployment of industry in order to avoid congestion and environmental problems."^4

---


The policy behind the fact that subsidies are addressed in international agreements is that they create a distortion in international trade and that they "can quickly and destructively spread from nation to nation."^5 They create "a disparity between the actual costs incurred in producing a particular good and those which must be borne by the firm undertaking its production."^6 But because the concentrated interests of producers command greater political support than the diffuse interests of consumers, national governments find it much easier to emulate the vices of protection than the virtues of free trade. This lesson has prompted the international community to fashion guidelines that distinguish between acceptable and unacceptable national subsidy measures and to codify those guidelines both in bilateral treaties and in multilateral agreements.^7

Subsidies are in international trade parlance referred to as 'domestic' and 'export' subsidies. A "domestic subsidy is granted to an industry on all of its production if a product, regardless of whether that production is

^4 Id. at art. 11(1).
^7 Hufbauer & Shelton, supra note 5, at 5-6.
exported." \(^8\) "An export subsidy, by contrast, is paid to an industry only on products that are exported." \(^9\)

This thesis deals in particular with the treatment of domestic subsidies in the WTO Agreement on Subsidies and Countervailing Measures (SCM Agreement) \(^10\) and the imposition of countervailing duties to offset them under Section 701 of the Tariff Act of 1930 \(^11\).

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\(^9\) Id. at 758.


article or merchandise from such country ..., then upon the importation of any such article or merchandise into the United States ... there shall be levied and paid ... and additional duty equal to the net amount of such bounty or grant ...."\textsuperscript{13} This general countervailing duty law was extended in 1922 to cover domestic subsidies. The Fordney-McCumber Tariff provided "that whenever any country ... shall pay or bestow ... any bounty or grant upon the manufacture or production or export of any article or merchandise manufactured or produced in such country ..., then upon the importation of any such article or merchandise into the United States ... there shall be levied and paid ... an additional duty equal to the net amount of such bounty or grant ...."\textsuperscript{14}

The Tariff Act of 1922 was the predecessor of the Tariff Act of 1930\textsuperscript{15}. Title VII of the Tariff Act of 1930 is now applicable to the imposition of countervailing duties and

\textsuperscript{12} Tariff Act of 1890, ch. 1244, sec. 237, 26 Stat. 584 (1890) (repealed or otherwise superseded by Internal Revenue Code of 1939, sec. 4, 53 Stat. 1 (1939)).

\textsuperscript{13} Tariff Act of 1897, ch. 11, sec. 5, 30 Stat. 205 (1897) (repealed or otherwise superseded by Internal Revenue Code of 1939, sec. 4, 53 Stat. 1 (1939)).


\textsuperscript{15} Tariff Act of 1930, ch. 497, 46 Stat. 590 (1930).
will be scrutinized in detail in Chapter IV of this thesis.

The United States are and have been the country with the most countervailing measures taken to offset trade distortions caused by subsidies as the following table shows:

**Summary of countervailing duty actions, 1997**

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<tr>
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</thead>
<tbody>
<tr>
<td>Argentina</td>
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</tr>
<tr>
<td>United States</td>
<td>6</td>
<td>0</td>
<td>52</td>
</tr>
</tbody>
</table>

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B. GATT: Articles VI, XVI and XXIII

The first time subsidies were addressed in a multilateral agreement was in the General Agreement on Tariffs and Trade (GATT). The basic obligations concerning subsidies are contained in GATT Article XVI.

GATT Article XVI:1 sets out a reporting requirement "if any contracting party grants or maintains any subsidy, including any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory." Furthermore, GATT Article XVI states restraints on export subsidies by requiring the "contracting parties [to] seek to avoid the use of subsidies on the export of primary products." If, however, a contracting party grants export subsidies on primary products, its obligation is set out in

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18 Id. at art. XVI.
19 Id. at art. XVI:3.
GATT Article XVI:3, which states that export subsidies on primary products "shall not be applied in a manner which results in that contracting party having more than an equitable share of world export trade in that product."\(^{20}\) With respect to subsidies on non-primary products, GATT Article XVI:4 requires that "contracting parties shall cease to grant either directly or indirectly any form of subsidy on the export of any product other than a primary product which subsidy results in the sale of such product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market."\(^{21}\) Thus GATT Articles XIV:3 and XIV:4 did not directly prohibit subsidies but set out the mere obligation to avoid and cease the use of subsidies. Domestic subsidies were not addressed directly at all in GATT Article XVI.

A reference to domestic subsidies was made in the Report of the Working Party on "Other Barriers to Trade", adopted in the 1954-1955 review session, relating to the The Nullification and Impairment of Benefits (GATT Article XXIII). The Report stated that

\(^{20}\) Id.  
\(^{21}\) Id. at art. XVI:4.
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.  

That means that although domestic subsidies were not prohibited under GATT Article XVI, they can constitute an impairment of benefits accruing to a contracting party. In a decision concerning subsidies paid to processors and producers of oilseeds by the European Economic Community the GATT Dispute Settlement Body (Panel) found that benefits accruing to the United States under Article II of the General Agreement in respect of the zero tariff bindings for oilseeds in the Community Schedule of Concessions were impaired as result of the introduction of production subsidy schemes which operate to protect Community producers of oilseeds completely from the movement of prices of imports and thereby prevent the tariff concessions from having any impact on the competitive relationship between domestic and imported oilseeds.  

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23 Decisions and Reports, Report by the Panel on "European Economic Community - Payments and Subsidies paid to Processors and Producers..."
The panel rejected the argument that since "[GATT] Articles III:8(b) XVI:1 explicitly recognize the right of contracting parties to grant production subsidies,"\(^{24}\) there can be no impairment. On the other hand, the panel agreed with a former decision concerning subsidies on ammonium sulphate stating that nothing in [GATT] Article XXXIII ... would empower the CONTRACTING PARTIES to require a contracting party to withdraw or reduce a consumption subsidy .... The ultimate power of the CONTRACTING PARTIES under [GATT] Article XXIII is that of authorizing an affected contracting party to suspend the application of appropriate obligations or concessions under the General Agreement.\(^{25}\)

The GATT therefore provided no direct means to restrict the use of domestic subsidies. Besides the withdrawal of concessions under GATT Article XXIII contracting parties were authorized to respond to the use of (domestic) subsidies in the form of countervailing duties.

GATT Article VI deals with the imposition of antidumping and countervailing duties under the GATT.

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\(^{24}\) Id. at 128.

GATT Article VI:4 defines "countervailing duty" as "a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, either directly or indirectly, upon the manufacture, production or export of any merchandise," and limits the amount of any countervailing duty imposed by a contracting party to "an amount equal to the estimated bounty or subsidy determined to have been granted."\(^{26}\)

GATT Article VI:6(a) establishes that a contracting party may not impose countervailing duties on imports of another contracting party unless it determines that the subsidization "is such as to cause or threaten material injury to an established domestic industry, or is such to retard materially the establishment of a domestic industry."\(^{27}\) However, because GATT Article VI was subject to grandfather rights, this injury test did not apply to the United States countervailing duty law because it predated the adoption of the GATT and did not contain the requirement of an injury test.

\(^{26}\) GATT, supra note 17 at art. VI:4.

\(^{27}\) Id. at art. VI:6(a).
C.  **Tokyo Round Negotiations: The Subsidies Code**

These flaws of the original GATT were tried to be eliminated by the negotiation of the Subsidies Code in the Tokyo Round negotiations from 1974 through 1979. The Tokyo Round negotiations were aimed, "inter alia, to...reduce or eliminate non-tariff measures or, where this is not appropriate, to reduce or eliminate their trade restricting or distorting effects, and to bring such measures under more effective international discipline,..."\(^{28}\)

"The objective of the United States in the negotiations was to strengthen the rules of the General Agreement on Tariffs and Trade (GATT) governing subsidy practices."\(^{29}\)

The Report of the Senate Finance Committee on the Trade Act of 1974\(^{30}\) set the goal:

In the long run, United States interests will be best served by an international agreement to eliminate subsidies which distort world trade patterns and discriminate against United States sales both at home and abroad. Central to the forthcoming multilateral


negotiations should be the establishment of acceptable international rules governing the use of subsidies.\textsuperscript{31}

Most of the other participants negotiations, however, saw the use of subsidies expressly designed to stimulate exports as strictly a question of national internal policy. According to this viewpoint, only when a country's trade or production was injured by a particular subsidy practice did that country have a legitimate ground to raise a concern. Thus, far from needing stronger rules on subsidies, the problem, as most MTN participants saw it, was to have the United States accept discipline, in the form of a material injury test, over its countervailing duty action.\textsuperscript{32}

The Tokyo Round negotiations led to a compromise between the United States and other participants concerning application of an injury test by the United States and the recognition by the other participants that domestic subsidies can have injurious effects and that countervailing measures should be allowed against them.

The Subsidies Code sets up a two-track approach to disciplining subsidies. Track I deals entirely with countervailing duties, establishing international rules on what national government can do in implementing their countervailing duty rules (including constraints on the


\textsuperscript{32} RIVERS & GREENWALD, supra note 29, at 1449.
procedures for those cases) and defining what constitutes a material injury. Track II of the Subsidies Code is devoted to the substantive obligations under international law regarding how governments should refrain from granting subsidies that affect goods in international trade.

In Track I the Subsidies Code recognizes a Signatory's right to impose countervailing duties on subsidized imports that cause injury to its domestic producers. Article 2:1 of the Subsidies Code sets out that "[c]ountervailing duties may only be imposed pursuant to investigations initiated and conducted in accordance with the provisions of this Article. An investigation to determine the existence, degree and effect of any alleged subsidy shall normally be initiated upon a written request by or on behalf on an industry affected."33

In Track II the Subsidies Code sets out the obligations of the Signatories concerning the use of subsidies. Article 9:1 of the Subsidies Code states that "[s]ignatories shall not grant export subsidies other than certain primary products."34 That goes beyond GATT Article XVI:4, which sets out the mere obligation to

33 SCM Agreement, supra note 10 at art. 2:1
34 Id. at art. 9:1.
cease the grant of subsidies if they meet the bi-level pricing condition.

In Article 10:1 of the Subsidies Code the Signatories agreed “not to grant directly or indirectly any export subsidy which results in the signatory granting such subsidy having more than an equitable share of world export in such product, ....”\(^{35}\)

The retention of differential treatment for primary and non-primary products was due to large subsidies in the agricultural sector that were a central part of the European Communities Common Agricultural Policy\(^ {36}\). In further negotiations subsidies on agricultural products were treated with separately.

Rules governing the use of export subsidies and the imposition of countervailing measures were not the sole focus of the Subsidies Code. The Signatories recognized in Article 11:1 of the Subsidies Code “that subsidies other than export subsidies are widely used as important instruments for the promotion of social and economic policy objectives and do not intend to restrict the right of signatories to use such subsidies to achieve these and other important policy objectives which they consider

\(^{35}\) Id. at art. 10:1

\(^{36}\) See RIVERS & GREENWALD, supra note 29 at 1448.
desirable."\textsuperscript{37} At the same time, however, the Signatories recognized, "that subsidies other than export subsidies ... may cause or threaten to cause injury to a domestic industry of another signatory .... Signatories shall therefore seek to avoid causing such effects through the use of subsidies."\textsuperscript{38}

Thus the Subsidies Code did not accomplish an agreement on the disciplining of domestic subsidies. Furthermore, the Subsidies Code did not contain a definition of a subsidy, which led to confusion in imposing countervailing measures, which may be levied only to offset subsidies. In the United States, the Court of International Trade (CIT) established the specificity test to determine when a government aid amounted to a subsidy\textsuperscript{39}, but the Subsidies Code provided no direct guidelines in this respect. The Subsidies Code contained an illustrative list of export subsidies in its annex indeed, but this list was not exhaustive and gave only a hint when governmental aid is specific enough to be subsidy:

- "Signatories recognize that the objectives mentioned in paragraph 1 above [of Article 11 of the Subsidies

\textsuperscript{37} SCM Agreement, \textit{supra} note 10 at art. 11:1.

\textsuperscript{38} Id. at art. 11:2.
Code] may be achieved, inter alia, by means of subsidies granted with the aim of giving an advantage of certain enterprises."^40

- "The provision by governments of direct subsidies to a firm or an industry contingent upon export performance."^41

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^40 SCM Agreement, supra note 10 at art. 11:3.

^41 Id. at Annex(a).
III. The Uruguay Round: The Agreement on Subsidies and Countervailing Measures

Although the Subsidies Code was an important step toward disabling nations from frustrating tariff concessions through the use of non-tariff measures it still did not contain a direct prohibition on domestic subsidies and, more important a definition of a subsidy. After completion of the Tokyo Round, the new Subsidies Code was subject to review and interpretation by the GATT Subsidies and Countervailing Measures Committee. The weaknesses of the Subsidies Code were presented in a Note prepared by the Secretariat for the subsidies negotiating group in the Uruguay Round:

Divergent views have been expressed regarding the question as to whether a financial contribution by a government should be one of the criteria for determining the existence of a countervailable subsidy .... Conflicting views have been put forward on the question whether a necessary condition for the existence of a countervailable (domestic) subsidy is that the practice in question confers a net benefit to the recipient and
adversely affects the conditions of normal competition ...

The fundamental problem which has prevented the signatories from reaching agreement on the methodology to calculate the amount of a subsidy is the divergence of views on the question whether the measure of the amount of the subsidy is the cost to the government providing that subsidy or the benefit of the recipient of that subsidy.\footnote{Problems in the Area of Subsidies and Countervailing Measures, Note by the Secretariat, GATT Doc. No. MTN.GNG/NG10/W/3 (March 17, 1987).}

These particular deficits concerning subsidies and much more importantly the weakness of the GATT's dispute settlement authority led in November 1985 to the establishment of a Preparatory Committee "to determine the objectives, subject matter, modalities for and participation in the multilateral trade negotiations ..."\footnote{Decision of 28 November 1985 on Establishment of the Preparatory Committee, GATT B.I.S.D. (32nd Supp.) at 10 (1986).}

This round of negotiations, termed the Uruguay Round, was launched in Punta del Este, Uruguay in September 1986.

The major achievement of the Uruguay Round was the Agreement establishing the World Trade Organization\footnote{Marrakech Agreement establishing the World Trade Organization (WTO) and related Agreements, April 15, 1994, Uruguay Round Agreement Act, PL 103-465, sec. 101(d)(2), 108 Stat. 4809, reprinted in JOHN H. JACKSON ET AL., 1995 DOCUMENTS SUPPLEMENT TO LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS, 3 (3rd ed. 1995).}, which contained in its Annex the Agreement on Subsidies...
and Countervailing Measures\textsuperscript{45}. Unlike the 1979 Tokyo Round Subsidies Code, which only 24 countries joined, all countries that become members of the WTO automatically become members of the SCM Agreement. The SCM Agreement addresses two separate but closely related topics: Multilateral disciplines regulating the provision of subsidies, and the use of countervailing measures to offset injury caused by subsidized imports. Multilateral disciplines are the rules regarding whether or not a subsidy may be provided by a Member. They are enforced through invocation of the WTO dispute settlement mechanism. Countervailing duties are an unilateral instrument, which may be applied by a Member after an investigation by that Member and a determination that the criteria set forth in the SCM Agreement are satisfied.

A. Definition of a subsidy

Unlike the Subsidies Code, the SCM Agreement contains a definition of the term subsidy. Article 1 of the SCM Agreement requires two elements: (1) a "financial

\textsuperscript{45} See SCM Agreement, supra note 10.
contribution by a government or any public body” ⁴⁶ within that government’s territory and (2) the conferral of a “benefit” ⁴⁷.

Four categories of practices that constitute a financial contribution are specified in Article 1.1(a)(1) of the SCM Agreement: (1) “a direct transfer of funds (e.g., grants, loans, and equity infusions)” ⁴⁸ or “potential direct transfers of funds or liabilities (e.g., loan guarantees)” ⁴⁹; (2) “government revenue otherwise due that is foregone or not collected (e.g., fiscal incentives such as tax credits)” ⁵⁰; (3) government provision of goods and services other than general infrastructure ⁵¹. The fourth category is directed against the circumvention of the rules. Article 1.1(a)(1)(iv) of the SCM Agreement makes clear that a financial contribution can exist where, rather than acting directly, “a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions [described] above, which normally would’be vested in the

⁴⁶ Id. at art. 1.1(a)(1).
⁴⁷ Id. at art. 1.1(b).
⁴⁸ Id. at art. 1.1(a)(1)(i).
⁴⁹ Id.
⁵⁰ Id. at art. 1.1(a)(1)(ii).
⁵¹ See Id. at art. 1.1(a)(1)(iii).
government, and the practice, in no real sense, differs from practices normally followed by governments."

Thus, the SCM Agreement solved the dispute over the concept of ‘financial contribution’ by adopting the approach that there could be no subsidy unless there was a charge on the public account. Other forms of government intervention that do not involve expense to the government do not constitute a subsidy. The other point of controversy, whether the existence of a benefit should be assessed with reference to a commercial benchmark (benefit-to-the-recipient methodology) or with reference to the cost to the subsidizing government (cost-to-the-government standard) was not solved in favour of one of the approaches. The cost-to-the-government standard is used to calculate the amount of subsidies regarding the threshold of an actionable subsidy, whereas the benefit-to-the-recipient standard is used to calculate the amount of subsidies in countervailing duty proceedings.

52 Id. at art. 1.1(a)(1)(iv).
B. Specificity

After the Uruguay Round, for the first time specificity was made a requirement under the GATT. Assuming that a measure is a subsidy within the meaning of the SCM Agreement, it nevertheless is not subject to the SCM Agreement unless it has been specifically provided to an enterprise or industry or group of enterprises or industries. The basic principle is that a subsidy that distorts the allocation of resources within an economy should be subject to discipline. Where a subsidy is widely available within an economy, such a distortion in the allocation of resources is presumed not to occur. Thus, only 'specific' subsidies are subject to SCM Agreement disciplines.

Article 2.1 of the SCM Agreement sets out de jure and de facto grounds to determine the specificity of a subsidy. Article 2.1(a) of the SCM Agreement provides that a subsidy shall be specific "[w]here the granting authority ... explicitly limits access to a subsidy to certain enterprises."53 That means on the other hand, as Article 2.1(b) of the SCM Agreement lays down, that

53 Id. at art. 2.1(a).
"[w]here the granting authority ... establishes objective criteria or conditions governing the eligibility for, and the amount of, a subsidy, specificity shall not exist ...."\(^5^4\)

Article 2.1(c) of the SCM Agreement provides that notwithstanding the absence of de jure grounds for a finding of specificity, where there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. They are: (1) the "use of a subsidy program by a limited number of certain enterprises"\(^5^5\) (industry specificity); (2) the "predominant use by certain enterprises"\(^5^6\) (enterprise-specificity); (3) "the granting of disproportionately large amounts to certain enterprises"\(^5^7\); and (4) "the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy."\(^5^8\)

Article 2.3 of the SCM Agreement provides that prohibited subsidies according to Article 2 of the SCM Agreement are automatically deemed to be specific.\(^5^9\)

Recognizing the federal structure of some Signatories, 

\(^5^4\) Id. at art. 2.1(b).
\(^5^5\) Id. at art. 2.1(c).
\(^5^6\) Id.
\(^5^7\) Id.
\(^5^8\) Id.
\(^5^9\) See id. at art. 2.3.
Article 2.2 of the SCM Agreement provides that central
government subsidies limited to a region are specific,
even if generally available throughout the region.\(^60\) That
means on the other hand that subsidies granted by a state
or province on a generally available basis within a state
or province (i.e., not limited to certain enterprises
within a state or province) are not specific.

The purpose of the specificity test is to function as an
initial screening mechanism to winnow out only those
foreign subsidies with truly are broadly available and
widely used throughout an economy. The application of the
specificity test in United States countervailing duty law
will be discussed in detail in Chapter IV of this thesis.

C. Classes of Subsidies

Articles 3 to 9 of the SCM Agreement establish a three-
class framework for the categorization of subsidies and
subsidy remedies: (1) subsidies that are prohibited (the
'red light' category); (2) subsidies that may be
challenged in WTO dispute settlement proceedings and
domestically countervailed if they cause adverse trade

\(^60\) See id. at art. 2.2.
effects (the ‘yellow light’ category, including ‘dark amber’); and (3) subsidies that are non-actionable and non-countervailable if they are structured according to criteria intended to limit their potential for causing trade distortions (the ‘green light’ category).

The ‘traffic light’ framework was adopted from a Swiss suggestion at a meeting of the negotiating group in February 1988. Switzerland proposed to “redefine existing categories and to introduce three different classes of subsidies: prohibited subsidies, actionable subsidies and non-actionable subsidies.”

1. **Prohibited (‘Red Light’) Subsidies**

Article 3 of the SCM Agreement lists two categories of subsidies that are prohibited under all circumstances. The first is “subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance ...” (export subsidies). A detailed

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61 See Meeting of 1-3 February 1988, Note by the Secretariat, GATT Doc. Nr. MTN.GNG/NG10/6 (Feb. 15, 1988).


63 SCM Agreement, supra note 10 at art. 3.1(a).
list of export subsidies is annexed to the SCM Agreement. The second is "subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods" (local content subsidies). These two categories of subsidies are prohibited because they are designed to affect trade and thus are most likely to have adverse effects on the interests of other members.

The scope of these prohibitions is relatively narrow. Developed countries had already accepted the prohibition on export subsidies under the Subsidies Code, and the local content subsidies of the type prohibited by the SCM Agreement were inconsistent with the National Treatment Clause in GATT Article III:1, which provided that "[t]he products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use." What is most significant about the SCM Agreement concerning export

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64 See id. at Annex 1.
65 Id. at art. 3.1(b).
66 GATT, supra note 17 at art. III:4.
subsidies is the extension of the obligations to developing country Members in accordance with specified transition rules, as well as the creation in Article 4 of the SCM Agreement of a rapid (three-month) dispute settlement mechanism for complaints regarding prohibited subsidies. All that must be established is the existence of a prohibited subsidy. If a panel or the Appellate Body finds that a government is maintaining a prohibited subsidy, the Dispute Settlement Body of the WTO must authorize countermeasures if the subsidy is not withdrawn expeditiously.

2. Actionable ('Yellow Light' and 'Dark Amber') Subsidies

Most subsidies, such as production subsidies fall into the 'actionable' category. Actionable subsidies are not prohibited. However, they are subject to challenge, either through multilateral dispute settlement or through countervailing action, in the event that they cause adverse effects to the interests of another Member.

67 See SCM Agreement, supra note 10 at art. 4.
Article 5 of the SCM Agreement sets out three types of adverse effects:

"(a) injury to the domestic industry of another Member;
(b) nullification or impairment of benefits accruing directly or indirectly to other [WTO] Members ...;
(c) serious prejudice to the interests of another Member."^68

Unlike the Subsidies Code, Article 6 of the SCM Agreement defines the term 'serious prejudice'. A major improvement to the Subsidies Code is that 'serious prejudice' cannot only arise as a result of adverse effects in the market of the importing Member but also in a third country market. Article 6.3(b) of the SCM Agreement provides that "[s]erious prejudice ... may arise in any case where ... the effect of the subsidy is to displace or impede the exports of a like product in another Member from a third country market."^69

The SCM Agreement refers to two kinds of actionable subsidies against which action can be taken in the WTO or in domestic countervailing duty proceedings if adverse effects are established by an effected Member. The first type are those dealt with by the SCM Agreement as

^68 Id. at art. 6.
^69 Id. at art. 6.3(b).
prohibited or non-actionable subsidies and for which, in the case of a serious prejudice, non-exhaustive examples are provided in Article 6.3 of the SCM Agreement. The second type (termed ‘dark amber’ subsidies), listed in Article 6.1 of the SCM Agreement, are presumed to cause serious prejudice. Where serious prejudice is presumed, Article 6.2 of the SCM Agreement places the burden on the subsidizing government to demonstrate that serious prejudice did not result from the subsidization in question. The four ‘dark amber’ subsidies are:

“(a) the total ad valorem subsidization of a product exceeding 5 per cent;
(b) subsidies to cover operating losses sustained by an industry;
(c) subsidies to cover operating losses sustained by an enterprise, other than one-time measures which are non-recurrent and cannot by repeated for that enterprise and which are given merely to provide time for the development of long-term solutions and to avoid acute social problems;
(d) direct forgiveness of debt ....”\(^{70}\)

\(^{70}\) Id. at art. 6.1.
Annex IV of the SCM Agreement sets forth general rules governing how a complaining member is to calculate the total ad valorem subsidization of a product for purposes of showing whether the 5 per cent threshold of Article 6.1(a) of the SCM Agreement has been reached. The most fundamental of the general rules set forth in Annex IV is the broad statement in Paragraph 1 that the ad valorem calculation must be based on the cost-to-the-government measurement standard. Annex IV Paragraph 1 of the SCM Agreement provides that "[a]ny calculation of the amount of a subsidy for the purpose of paragraph 1(a) of Article 6 shall be done in terms of the cost to the granting government."\(^{71}\)

That causes a number of problems since the cost-to-the-government standard is not further explained in the SCM Agreement in contrary to Article 14 of the SCM, which endorses the benefit-to-the-recipient standard for use in countervailing duty proceedings. Further questions are whether the overall rate of subsidization should be calculated separately for each benefiting company or whether the overall rate of subsidization must be calculated as an aggregate for all benefiting companies.

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\(^{71}\) Id. at Annex IV, § 1.
The other problem is whether Red Light subsidies should be included in the calculation of the overall rate of subsidization.

Remedies against actionable subsidies are laid out in Article 7 of the SCM Agreement. Once a Member requests consultations regarding such a subsidy, the SCM Agreement allots 180 days for completion of the panel proceedings and the issuance of a decision by the Dispute Settlement Body. The SCM Agreement provides an additional 60 days for appeals of panel findings. The Dispute Settlement Body must authorize countermeasures where a Member has not either withdrawn a subsidy found to be causing serious prejudice or eliminated its adverse effects within six months.

3. Non-Actionable ('Green Light') Subsidies

The SCM Agreement accords non-actionable, or 'Green Light', status to three narrow types of subsidies. That means those subsidies cannot be challenged multilaterally or be subject to countervailing action. These subsidies presumably are protected either because they are considered extremely unlikely to cause adverse effects or
because they are considered to be of particular value and not to be discouraged. Article 8 of the SCM Agreement provides for three types of non-actionable subsidies:

(a) basic research and pre-competitive development subsidies;\(^7^2\)
(b) assistance to disadvantaged regions;\(^7^3\)
(c) assistance to adapt existing facilities to new environmental requirements.\(^7^4\)

Under Article 8.2(a) of the SCM Agreement, government assistance for research activities conducted by firms, or by higher education or research establishments on a contract basis with firms, is non-actionable if the assistance does not exceed a designated proportion of project costs and is only used for certain expenditures.

Under Article 8.2(b) of the SCM Agreement, government assistance to disadvantaged regions is non-actionable if it is not limited to specific enterprises or industries within the region, given pursuant to a general scheme of regional development, and the region is disadvantaged by comparison with the Member as a whole in terms of

\(^7^2\) See id. at art. 8.2(a).
\(^7^3\) See id. at art. 8.2(b).
\(^7^4\) See id. at art. 8.2(c).
objective criteria such as GNP per capita and unemployment.

Under Article 8.2(c) of the SCM Agreement, government assistance for environmental adaptation is considered permissible if it is given on a one-time basis, limited to 20 per cent of adaptation costs, and available to all firms which can adopt the new equipment and processes.

D. Rules regarding countervailing duty proceedings

Articles 10 through 23 (Part V) of the SCM Agreement establish rules for domestic countervailing duty proceedings. Part V of the SCM Agreement sets forth certain substantive requirements that must be fulfilled in order to impose a countervailing measure, as well as in-depth procedural requirements regarding the conduct of a countervailing investigation and the imposition and maintenance in place of countervailing measures. A failure to respect either the substantive or procedural requirements of Part V can be taken to dispute settlement and may be the basis for invalidation of the measure.

A Member may not impose a countervailing measure unless it determines that there are subsidized imports, injury to
a domestic industry and a causal link between the subsidized imports and the injury.

As laid out in Chapter III.B of this thesis, a subsidy is countervailable only if it is specific. This thesis focuses in Chapter IV on this first step of a countervailing measure procedure, in particular how the specificity test is implemented in U.S. domestic countervailing duty law.

Part V of the SCM Agreement furthermore contains detailed rules regarding the initiation and conduct of countervailing investigations, the imposition of preliminary and final measures, the use of undertakings, and the duration of measures.
IV. U.S. Legislation

The Uruguay Round Agreements Act implemented the SCM Agreement into U.S. countervailing duty law.\textsuperscript{75} The Uruguay Round Agreements Act did not alter the procedure that had been imposed by The Trade Agreements Act of 1979.\textsuperscript{76}

The Trade Agreements Act of 1979 imposed a two-step test that must be satisfied before a countervailing duty can be used against a Member. The first step requires that the Commerce Department determines whether a subsidy even exists.\textsuperscript{77} Then, if there is a subsidy, the International Trade Commission (ITC)\textsuperscript{78} must determine whether there has been a material injury to an U.S. industry.\textsuperscript{79}

Chapter IV of this thesis focuses on the first step of this test, the determination of the existence of a subsidy.


\textsuperscript{76} The Trade Agreements Act of 1979, Pub. L. No. 96-39, 93 Stat. 144 (codified as amended in scattered sections of 19 U.S.C.). This law was passed in response to the Tokyo Round of the GATT.


\textsuperscript{78} Hereinafter ITC.

A. Basic Definition

Section 771(5)(A) of the Act provides the basic definition of the terms 'subsidy' and 'countervailable subsidy'. The systematic of the provision is to provide a definition of a subsidy according to Article 1 of the SCM Agreement in section 771(5)(B) of The Act and to restrict in section 771(5A) of the Act the admissibility of countervailing measures to subsidies that are specific according to Article 2 of the SCM Agreement.

With respect to the term subsidy, section 771(5)(B) of the Act tracks the language of Article 1 of the SCM Agreement. It provides that a subsidy exists where "a government of a country or any public entity within the territory of the country"  

(i) provides a financial contribution,

(ii) provides any form of income or price support within the meaning of Article XVI of the GATT 1994, or

(iii) makes a payment to a funding mechanism to provide a financial contribution, or entrusts or directs a private entity to make a financial contribution, of providing the contribution
would normally be vested in the government and the practice does not differ in substance from practices normally followed by governments, ...."  

The definition of a financial contribution is to be found in Section 771(5)(D) of The Act, which tracks the language of Article 1 of the SCM Agreement. A problematic issue in determining whether a subsidy exists is whether Article 1.1(a)(1)(iv) of the SCM Agreement and Section 771(5)(B)(iii) of the Act encompass indirect subsidy practices.

Those practices can vary widely but one practice appeared frequently in the past, which does not seem to fall in one of the prongs of the definition. These cases involved export restraints that artificially raised the domestic supply of a certain good.

In *Leather from Argentina*, the Department of Commerce issued a Countervailing Duty Order to offset subsidies that were conferred to manufacturers, producers, or exporters in Argentina of leather. In 1972, the Government of Argentina implemented an embargo on the export of cattle hides. The Department of Commerce found

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81 Id.
that prices for cattle hides in Argentina were considerable lower when the embargo was in force. The lower price for cattle hide in Argentina benefited domestic producers of leather but was not directly caused by the embargo but by the higher supply. The Department of Commerce determined that the Argentina cattle hide embargo is countervailable nonetheless, because there was “a cognizable and discernible link between the Argentina hide embargo” and the low domestic price for cattle hide.

The rationale underlying that determination was that the export embargo “caused hide prices to be lower than they would have been absent the embargo” and, thereby, enabled the leather tanners to sell the finished product, leather, at a lower price.

The ‘direct and discernible effect’ standard was reapplied in Certain Softwood Lumber Products from Canada. This case involved the practice of Log Export Restrictions (LERs) used by the Government of British

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83 Id. at 40,213.
84 Id. at 40,214.
85 Id. at 40,213.
87 Hereinafter LER.
Columbia.\footnote{The Lumber Case dragged on for over twelve years. This controversy originally arose as a result of a Canadian 'stumpage pricing' policy, under which timber on government-owned lands is sold to private Canadian companies that pay a 'stumpage price' for the right to harvest it. In 1983, in response to a petition from a coalition of U.S. lumber producers, the Commerce Department found these practices not to be countervailable (Final Negative Countervailing Duty Determinations; Certain Softwood Products from Canada, 48 Fed. Reg. 24159 (1983)). When the coalition petitioned again in 1986, the Commerce Department reversed its previous findings and held in a preliminary determination that the stumpage system was a countervailable subsidy (Preliminary Affirmative Countervailing Duty Determination: Certain Softwood Lumber Products from Canada, 51 Fed. Reg. 37453-02 (1986)). Canada responded quickly with an offer of implementing a 15% export tax on all lumber in exchange for an agreement not to impose a countervailing duty. The Commerce Department agreed and declared that the preliminary finding was without effect, and the deal was finalized in a Memorandum of Understanding (See Memorandum, Determination under Section 301 of the Trade Act of 1974, 52 Fed. Reg. 233 (1986)). In 1991, Canada terminated the Agreement and the Department of Commerce initiated a countervailing duty investigation (Self-Initiation of Countervailing Duty Investigation: Certain Softwood Lumber Products from Canada, 56 Fed. Reg. 56055 (1991)). Included in the investigation was a new complaint about the practice of LERs in British Columbia. In 1992, the Commerce Department issued a final determination and imposed a countervailing duty based on both the stumpage practices and the LER System (Certain Softwood Lumber Products from Canada, supra note 86). The Commerce Department found that the stumpage system did benefit specific producers with preferential rates. It also found that the LERs are subsidies within the meaning of Section 771(5)(A) of The Act, 19 U.S.C.A. § 1677(5)(A) (1991) (current version at 19 U.S.C.A. § 1677(5)(A) (West Supp. 1998)).} The issue in Certain Softwood Lumber Products from Canada was the same as in Leather from Argentina since the government of British Columbia did not maintain direct control over the log prices though the imposition of its export restrictions. But the Department of Commerce found also in this case that the indirect scheme had the effect of reducing the production costs of British Columbia softwood lumber manufacturers. Therefore the LERs had "a direct and discernible effect upon the British
Columbia domestic price of logs and, thereby, confer a benefit upon British Columbia softwood lumber manufacturers ....”

The ‘cognizable and discernable effect’ standard is supported in legal respect by GATT Article VI:3. GATT Article VI:3 refers to subsidies that “have been granted, directly or indirectly, on the manufacture, production or export of ... [a] product.” That means that the words “entrusts or directs a private party” in Article 1.1(iv) of the SCM Agreement have to be interpreted broadly to cover governmental actions that have indirect effects through a private body.

In practical respect the standard is supported by the necessity to prevent the circumvention of the SCM Agreement. The standard is a reasonable means to determine whether a measure has a direct effect on the price of the input product, in the foregoing cases raw hides and unprocessed lumber, even though the effect upon the processed product, leather and processed lumber, is indirect. The requirement of the existence of a ‘discernable link’ between the measure and the result

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89 Certain Softwood Lumber Products from Canada, supra note 86, at 22610.

90 GATT, supra note 17, at art. VI:3.

91 SCM Agreement, supra note 10, at art. 1.1(iv).
secures that only those measures are countervailable that constitute a financial contribution within the meaning of Article 1.1 of the SCM Agreement.

B. Specificity

Section 771(5A) of The Act implements the provision of Article 2 of the SCM Agreement dealing with specificity. The specificity requirement ensures that programs conferring a broad, generalized benefit are not countervailable. For example, roads and schools for public use or tax credits available to all companies confer a generalized benefit and are thus not countervailable. On the other hand, programs that favor one or more market participants and are capable of distorting the relative allocation of resources to different sectors a country's economy, or are potentially trade distorting, are specific benefits.92

Three policy goals underlie the specificity test.

First, the test supposedly serves as a practical limit on the number of possible claims United States industries can bring against subsidies in foreign countries. Such a practical limit ... is needed because all industries in every country receive some direct or indirect government benefits. ...

Second, some scholars maintain that the specificity test minimizes the distortive effects of countervailing duties by separating subsidies which distort economic efficiency form those that do not. The economic theory of comparative advantage suggests that gains from international trade are maximized when countries export goods that they can produce relatively more efficiently than producers in other countries and import goods that other countries can produce more efficiently. A specific subsidy supposedly misallocates resources away from a country’s efficient industries into its inefficient ones, thereby raising prices for importers of the affected products. ...

Finally, the specificity test is based on notions of fairness regarding the appropriate role for government in the economy. United States producers generally consider it unfair to have to compete against foreign rivals run or propped by their governments when at home United States producers must follow the ‘survival of the most efficient’ rule of free competition.93

Although the specificity requirement was added to an international agreement only in 1994 with the adoption of the SCM Agreement after the Uruguay Round, U.S. countervailing duty law contained a specificity test since 1979. The Trade Agreement Act of 197994 added a specificity test into Section 771 of The Act, which was in

force until 1994, when it was changed by the Uruguay Rounds Agreements Act\textsuperscript{95}. The old Section 771(B) of The Act read: "In applying subparagraph (A) [which defines the term subsidy], the administering authority [The Department of Commerce], shall determine whether the bounty, grant, or subsidy in law or in fact is provided to a specific enterprise or industry, or group of enterprises or industries. Nominal general availability, under the terms of the law, regulation or program, or rule establishing a bounty, grant, or subsidy, of the benefits thereunder is not a basis for determining that the bounty, grant, or subsidy is not, or has not been, in fact provided to a specific enterprise or industry, or group thereof."\textsuperscript{96}

Based on the statutory definition of a domestic subsidy, the Department of Commerce and the United States Court of International Trade\textsuperscript{97} (CIT) developed a specificity test to determine whether a government program constitutes a domestic subsidy. The specificity test states that only a government program conferring benefits on specific

\textsuperscript{94}See The Trade Agreements Act of 1979, \textit{supra} not 76.

\textsuperscript{95}See Uruguay Round Agreements Act, \textit{supra} note 75.


\textsuperscript{97}Hereinafter CIT.
enterprises or industries is a domestic subsidy.96 Thus, a government program generally available to many or all producers in the country is not a domestic subsidy giving rise to countervailing duties. These of court decisions still serve as guidelines in the interpretation of the new Section 771(5A) of the Act, which replaced Section 771(5)(B) of the Act.

In Carlisle Tire and Rubber Co. v. United States, which was decided in 1983, the CIT found the specificity test to a reasonable interpretation of the statute.99 In this case the Department of Commerce had determined that a generally available Korean tax law permitting accelerated depreciation that benefited a particular Korean manufacturer was not a bounty or grant.100 The CIT noted that application of a broad definition of bounty or grant would lead to the "absurd result" that almost all imports could be countervailed, a result that would create an overwhelming administrative burden and make impossible the

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96 Carlisle Tire and Rubber Co. v. United States, supra note 39 (upholding Department of Commerce's determination that a government program was not a subsidy within the meaning of countervailing duty law unless conferring a benefit upon a specific enterprise or industry); Cabot Corp. v. United States, 9 C.I.T. 489 (1985) (holding that a government program is not countervailable unless it bestows a benefit on a specific class of industries), appeal dismissed, 788 F.2d 1539 (Fed. Cir. 1986); PPG Industries v. United States, 11 C.I.T. 344 (1987) (same holding).

99 See Carlisle Tire and Rubber Co. v. United States, supra note 39.

100 Id. at 230, 231.
calculation of benefits. The CIO stated that if "generally available benefits are a bounty or grant... countervailable benefits would be such things as public highways and bridges, as well as a tax credit or expenditures on capital investment even if available to all industries and sectors." Thus, the CIO interpreted the "specificity" language in the Act as to limit "bounty or grant" to preferential subsidies.

The specificity test as applied in Carlisle Tire and Rubber Co. v. United States referred only to the de jure specificity of a certain subsidy. It did not take into consideration the intent of a government to target specific enterprises or industries with aids that were tailored to be generally available. "It specifically disregarded the fact that assistance that relieves a firm of a cost inherent to manufacture or production is a countervailable subsidy, regardless of the extent of subsidization or the generality of a foreign government." 14

14 Id. at 233, 234.
15 Id. at 233.
16 Id. at 638.
The first case to consider directly the validity of the specificity test was Bethlehem Steel Corp. v. United States. In this case, the South African government permitted companies to deduct 200 percent of their employee training program expenses from their income, a benefit the Department of Commerce held not to be a bounty or grand based on its general availability. The CIT upheld the specificity test in regard to tax provisions, but, in dicta, the CIT rejected the rationale "that, as a rule, generally available benefits are not subsidies." The CIT asked the rhetorical question whether it can "be argued that financial assistance that is inconsistent with commercial considerations it no longer a subsidy when it is part of the basic policy of a government and available to all businesses[]." In doing so the CIT purported a case-by-case approach:

In this decision the Court does not feel it is necessary to speak to a variety of practices which are not before the Court. It does not see the alternatives as being either the absurd assessment of countervailing duties on all beneficial acts of government or the exclusion from the effect of the law of all benefits which are

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106 See id. at 340.
107 Id. at 341.
108 Id. at 345.
generally available in a country. Both these extremes have their absurdities. The Court does not enter into broad policy formulations based on general economic tendencies in the world. In the early phases of the interpretation of difficult concepts of legislation ... it is best to keep the judicial results focused on the immediate factual pattern arising in each particular case.109

Those cases present two divergent approaches to the application of 'bounty or grant'.

On the one hand, Bethlehem Steel ... g[ave little deference to the ITA's interpretation of the statute it administers, finding the countervailing duty law to be clearly applicable to all domestic benefits regardless of whether they are preferential or not. On the other hand, Carlisle represents a deferential approach to what it considers a reasonable ITA interpretation of the statute based on legislative history, case law and economic analysis: domestic benefits are only countervailable when they are applied on a preferential basis to a specific economic sector or subsector.111

Despite this divergent approaches both theories have in common that the effect and the intent behind a benefit are to be examined.

109 Id. at 350.
In *Cabot Corp. v. United States* the CIT created a two-part test: first, whether a benefit actually accrues to a specific industrial beneficiary; second, whether the benefit confers a benefit, i.e., a 'competitive advantage'. ¹¹¹ This case arose out of Mexico's National Industrial Development Plan, which, utilizing incentives such as tax rebates, low interest loans and favorable energy rates, set investment priorities among industrial activities and geographic regions. ¹¹² The government of Mexico made carbon black feedstock available to its producers at well below world market prices; although the world market cost of petroleum feedstock was USD 26 per barrel, the Mexican government made petroleum feedstock available to Mexican producers at USD 2 per barrel. ¹¹³ Through the application of the specificity test, the Department of Commerce did not consider the Mexican natural resource subsidies to be countervailable. ¹¹⁴ The CIT overturned the Department of Commerce's decision and

¹¹⁰ Michael J. Sussmann, *Countervailing Duties and the Specificity Test: An Alternative Approach to the Definition of 'Bounty or Grant'*, 18 LAW & POL'Y INT'L BUS. 475, 494 (1986).


¹¹² See *id.* at 490.

¹¹³ See *id.*

¹¹⁴ See *id.* at 490, 491, 495.
found that this aspect of the Mexican National Industrial Development Plan constituted a subsidy.\textsuperscript{115}

The CIT found that the Department of Commerce had applied an incorrect legal standard, holding that when a government program, nominally available to all industries, only works to confer a benefit on specific enterprises or industries, the program meets the test for a countervailable subsidy.\textsuperscript{116} Thus the CIT distinguished between nominally and actually generally available subsidies:

The distinction that has evaded the ITA is not all so-called generally available benefits are alike — some are benefits accruing generally to all citizens, while others are benefits that when actually conferred accrue to specific individuals or classes. Thus, while it is true that a generalized benefit provided by government, such as national defense, education or infrastructure, is not a countervailable bounty or grant or grant, a generally available benefit — one that may be obtained by any and all enterprises or industries — may nevertheless accrue to specific recipients. General benefits are not conferred upon any specific individuals or classes, while generally available benefits, when actually bestowed, may constitute specific grants

\textsuperscript{115} See id. at 491.

\textsuperscript{116} See id. at 498.
conferred upon specific identifiable entities, which would be subject to countervailing duties.\textsuperscript{117}

The CIT then went on in developing the two-part test:

[The first inquiry is] whether a benefit or 'competitive advantage' has been actually conferred on a 'specific enterprise or industry, or group of enterprises or industries.' In the case before the Court, the availability of carbon black feedstock and natural gas at controlled prices does not determine whether the benefits actually received by these two carbon black producers are countervailable subsidies. ... Once it has been determined that there has been a bestowal upon a specific class, the second aspect of the definition of bounty or grant requires looking at the bestowal and determining if it amounts to an additional benefit or competitive advantage.\textsuperscript{118}

Thus, the two-part test is an inquiry into the issue whether an available benefit has an actual effect on the beneficiary. Thereby the CIT added to the specificity test the element of de-facto specificity.

This approach was reaffirmed in \textit{PPG Industries v. United States}.\textsuperscript{119} \textit{PPG Industries v. United States} involved the Fund for Promotion of Exports of Mexican Manufactured Products. The ITA determined that the Mexican

\textsuperscript{117} Id. at 497.

\textsuperscript{118} Id. at 498.
government's sale of natural gas to Mexican float glass producers at below world market prices did not amount to a countervailable subsidy because the natural gas was generally available to all Mexican industries. The CIT upheld the Department of Commerce's finding that "the float glass paid the published price for natural gas that was available to all industries and therefore received no countervailable benefit." The CIT stated that "the appropriate standard or test requires the agency to conduct a de facto case analysis to determine whether or not a program provides a 'subsidy' or a 'bounty or grant' to a 'specific enterprise or industry, or group of enterprises or industries.'" "PPG Industries thus clarified the Cabot rule to mean that when a government program is nominally generally available and in fact widely used, the program is not a countervailable subsidy."

121 PPG Industries v. United States, supra note 119, at 631.
122 Id. at 361, 362.
C. Section 771(5A)(D) of The Tariff Act of 1930

As stated above Section 771(5A)(D) of The Act replaced Section 771(B) of the Act and is far more detailed concerning the specificity of domestic subsidies. The statute provides definitions of de-jure and de-facto specificity, with which the standards under which the ITA conducts countervailing duty investigations have to be reconciled.

1. Specific Enterprise or Industry

The specificity test as laid out in Section 771(5A)(D) of The Act refers to the access of an industry or enterprise to a subsidy.\(^\text{124}\)

Whereas the definition of the term 'enterprise' causes no difficulties there is no definition of the term 'industry'. As the Department of Commerce stated in Certain Softwood Lumber Products from Canada, "there is a realm of acceptable definitions of the terms 'industry.'"\(^\text{125}\) In this case, the Department of Commerce


\(^{125}\) Certain Softwood Lumber Products from Canada, supra note 86, at 22584.
explicitly rejected the contention that product based
descriptions were applicable, or even helpful, in defining
the applicable industry or group.\textsuperscript{126} Similarly, in \textit{Certain Fresh Cut Flowers from the Netherlands}, the Department of
Commerce explicitly rejected the argument that benefits
provided to the horticulture and greenhouse industries
were too broad to be considered specific because they were
provided to more than sixty different categories of
products.\textsuperscript{127} The Department of Commerce thereby tends to
apply a common sense definition of industry based upon
practical experience and common usage.

Since the Department of Commerce is elusive in providing
a concrete definition of what constitutes an industry, a
more specific definition should be formulated. A
definition could consider such criteria as common
products, common unions, and common input.

2. \textit{De-jure Specificity}

Sections 771(5A)(D)(i) and (ii) of The Act cover de

\textsuperscript{126} Id. at 22584, 22585.

\textsuperscript{127} Final Affirmative Countervailing Duty Determination: Certain Fresh
jure-specificity and track the language of Articles 2.1(a) and (b) of the SCM Agreement.

Clause (i) provides that specificity exists where a government expressly limits eligibility for a subsidy to an enterprise or industry.\(^{128}\)

Clause (ii) is a corollary of the de jure test. Under clause (ii), a subsidy would not be deemed to be de jure specific merely it was bestowed pursuant to certain eligibility criteria. However, the eligibility criteria or conditions must be objective, clearly documented, capable of verification, and strictly followed. In addition, eligibility for the subsidy must be automatic where the criteria are satisfied. Finally, the objective must be neutral and must not favor certain enterprises or industries over others.\(^{129}\)

De jure specificity addresses legal, textual restrictions on the availability of a subsidy benefit. A clear-cut example of a de jure specific subsidy can be found in Live Swine from Canada.\(^{130}\) This case involved benefits to hog producers under the British Columbia Farm


Income Insurance Act.\textsuperscript{131} The Farm Income Insurance Act of 1973 listed in its Schedule B guidelines all products, whose producers are eligible to receive benefits under this program.\textsuperscript{132} The Department of Commerce found the program specific since "the program is limited to a specific group of enterprises or industries, and, therefore, is countervailable, because it is only available to farmers producing commodities under Schedule B guidelines of the Farm Income Insurance Act of 1973.\textsuperscript{133}

Questionable is whether de jure specificity exists only where the statute expressly specifies the benefiting industry or enterprise as a recipient of the subsidy or whether it is sufficient that one can establish the beneficiaries by analyzing the statute. The Department of Commerce applied in Certain Softwood Lumber Products from Canada the second interpretation.\textsuperscript{134} Although the statute did not explicitly set forth the beneficiaries of the program, the Department of Commerce found that the LER's "on their face, benefit only [British Columbia] users of logs ... Accordingly, the domestic benefits conferred by

\textsuperscript{131} See id. at 50563.
\textsuperscript{132} See id.
\textsuperscript{133} Id.
\textsuperscript{134} See Certain Softwood Lumber Products from Canada, supra 86 note at 22610.
these export restraints are de jure limited to a specific group of industries. ¹³⁵ This question is only academic though, since one can establish de facto specificity by furnishing evidence that a statute in fact benefits only one specific enterprise or industry.

De jure specificity does not exist, however, where a program merely restricts the access to certain benefits. The CIT found in PPG Industries v. United States the Mexican Trust Fund for Coverage of Risks (FICORCA) since sector neutral and objective factors formed the basis of criteria for eligibility, and if eligibility is automatic once these factors are met, then the program is not de jure specific even though eligibility may be limited on its face.¹³⁶ FICORCA was a trust fund set up by the Mexican government, which provided Mexican firms with registered debt in foreign currency an payable abroad with foreign currency at a controlled rate.¹³⁷ The CIT hold that "the mere fact that a program contains certain eligibility requirements for participation does not transform the program into one which has provided a countervailable benefit. The test necessarily involves

¹³⁵ Id.
¹³⁶ See PPG Industries v. United States, supra note 119, at 353.
¹³⁷ See id. at 350.
subjective case by case decisions to determine whether there is a discrete class of beneficiaries."

The concept of de jure specificity as applied by the Department of Commerce and adjudicated by the CIT provided the basis for the SCM regulation in Article 2.1(a) and (b) and its interpretation has therefore not to be changed to comply with the SCM Agreement.

3. **De facto Specificity**

Section 771(5A)D)(iii) of The Act lists the factors to be examined with respect to de facto specificity. These factors, tracking the language in Article 2.1(c) of the SCM Agreement, are:

"(I) The actual recipients of the subsidy, whether considered on an enterprise or industry basis, are limited in number.

(II) An enterprise or industry is a predominant user of the subsidy.

(III) An enterprise of industry receives a disproportionately large amount of the subsidy.

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138 See id. at 353.
(IV) The manner in which the authority providing the subsidy has exercised discretion in the decision to grant the subsidy indicates that an enterprise or industry is favored over others.\textsuperscript{139}

De facto specificity addresses the usage of a program's benefits by a specific enterprise or industry even if statutory and regulatory eligibility requirements are neutral and objective on their face, or if the benefits of a program are nominally available to the entire economy.

The concept of de facto specificity has been developed by a number of CIT decisions from Carlisle Tire and Rubber Co. to PPG Industries and focuses on the de facto access to the benefits of a program by a specific enterprise or industry. But there has been no definition at what point an enterprise or industry becomes the specific beneficiary of a subsidy. A de facto specificity test does make only little sense when it finds generally available a program that provides ninety-nine per cent of its benefit to a specific industry, even if the remaining one percent benefits dozens of industries. If the total number of beneficiaries is too broad, the relevant question then becomes how dominant or disproportionate is the specific

industry's use of the program's benefits. The SCM Agreement tries to clarify this issue by adding the terms 'dominant use' and 'disproportionate beneficiary' into the concept of de facto specificity.

a. Dominant Use

The dominant use analysis is based on the share of the benefit of a program to an enterprise or an industry. No set guidelines, however, exist for establishing dominant use.

In Certain Textile Mill Products and Apparel from Thailand, the Department of Commerce found in its preliminary determinations that an industry that availed itself for 45 percent of a program was specific based on dominant use. According to the Department of Commerce, approximately 45 percent of the rediscounts under this program were provided on the short-term promissory notes of producers of all products classified as textiles in Thailand. This percentage indicates that textile producers receive a disproportionate share of these rediscountable loans. Therefore, although there does not appear a de jure limitation within the program

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eligibility criteria, there does appear to be de facto limitation on the way in which the program operates.\textsuperscript{141}

This case involved the Bank of Thailand’s Regulations Governing the Rediscount of Promissory Notes Arising from Industrial Undertakings permitting commercial banks to rediscount short-term promissory notes for industrial purchases.\textsuperscript{142}

The use of the term ‘disproportionate’ does not have to be mistaken with the ‘disproportionate beneficiary’ analysis which will be discussed in Chapter IV.3.b of this thesis.

In its determination the Department of Commerce speaks of an indication and does not use a mathematical formula. Given the complex nature of this determinations and the differences in the industry structure of every country, a case-by-case determination seems to be the most reasonable approach. Nonetheless, the Department of Commerce should at least establish a framework for its analysis to provide guidance and reliability in its determinations.

\textsuperscript{141} Id.

\textsuperscript{142} See id.
b. Disproportionate Beneficiary

If not as a dominant user, an enterprise or industry can receive a disproportionate benefit under a program. Two arguments support this theory to deem an enterprise or industry as specific, although it is not the dominant user of benefit.

First, an industry may be receiving a disproportionate benefit, thus distorting the economy, when the share of its total use of the program's benefits is far greater than its contribution to the economy ... Second, one might argue that an industry receives a disproportionately large benefit compared with other users of a program. ¹⁴³

In Cold-Rolled Carbon Steel Flat-Rolled Products from Korea, the Department of Commerce used a ratio between the share of loans and industry received and that industry's share of the economy to determine that the steel industry was not receiving a disproportionate share of the medium- and long-term loans. ¹⁴⁴ This case involved medium- and long-term loans through government direction designed to finance major or key industries to Korean

¹⁴³ Ragosta & Shanker, supra note 92 at 668, 669.
¹⁴⁴ See Final Affirmative Duty Determination; Cold-Rolled Carbon Steel Flat-Rolled Products from Korea; and Final Negative Countervailing Duty Determination; Carbon Steel Structural Shapes from Korea, 49 Fed. Reg. 47284, 47289 (1984).
producers of shapes and sheet, as part of the Korean steel industry, which were made on terms that were inconsistent with commercial considerations.\textsuperscript{145} The Department of Commerce found that

\textit{[n]otwithstanding that certain of the sources have been created to provide credit to designated groups of recipients, these groups do not receive a disproportionate share of the total medium- and long-term credit available from all sources combined. Moreover, we determine that the steel industry does not receive a disproportionate share of funds from all these sources. Indeed, over the last 15 years, the steel industry has accounted for approximately 6 to 13 percent of GNP. During the same period the basic metals sector, which includes steel, has received 5 to 8 percent of medium- and long-term loans.}\textsuperscript{146}

In \textit{Certain Heavy Iron Construction Castings From Brazil,} the Department of Commerce again compared the ratio of percentage of GDP to the industry’s share of the benefit to find that no specificity existed.\textsuperscript{147} This case involved the Brazilian Fund for Developing of Mining and Metallurgy (FDM), which provided through the government-owned Development Bank of Minas Gerais (BDMG) loans to foundries

\textsuperscript{145} See Id.
\textsuperscript{146} Id.
on terms inconsistent with commercial considerations.\textsuperscript{148} Here the Department of Commerce found that mining and metallurgy together contributed over 51 percent to the Gross Domestic Product of the state, while receiving 33 percent of the credit extended by the BDMG in 1984. There is no evidence of targeting of these of other BDMG funds to the industry under investigation. Accordingly, we determine that loans under the FDM program are not limited to a specific enterprise or industry or group of enterprises or industries.\textsuperscript{149}

In the disproportionate beneficiary analysis the Department of Commerce does not use a set mathematical formula as well. A pragmatically case-by-case approach seems to be reasonable here, too, in order to take different economic situations in different countries into consideration. But the Department of Commerce should develop certain standards and framework in its determinations to make them reliable and reconstructable.

\textsuperscript{148} See id.

\textsuperscript{149} Id.
V. Conclusion

The SCM Agreement is a big step forward towards the elimination of subsidies. The SCM Agreement provides, compared to the GATT and the Subsidies Code, the means to tackle domestic subsidies, which potentially distort the allocation of resources in an economy. At the same token, the SCM Agreement recognizes that a) domestic subsidies can serve a purpose that justifies the misallocation of resources and b) specific subsidies rather than general, cross-industry subsidies should be singled out as countervailable since they favor certain market participants and distort the allocation of resources.

By deeming certain domestic subsidies as non-actionable, the SCM Agreement acknowledges certain policy objectives that are more important than ideal economic conditions. Research subsidies further scientific accomplishments in areas that are economically non-lucrative but benefit the society. Subsidies for disadvantaged regions equalize economic disparities in countries with disparate economic structures. In doing so, this kind of subsidies enhances
the quality of life in disadvantaged regions, which is viewed as more important than allocating resources in better suited regions even if this would be economically more reasonable. Environmental adaptation subsidies, the third category of non-actionable subsidies, serve the important goal of furthering environmental protection.

The specificity test serves the purpose of eliminating subsidies benefiting only particular enterprises or industries while allowing countries to subsidize the whole economy to achieve certain policy objectives not covered by Article 8 of the SCM Agreement to a de-minimis level of 5 percent. Problematic, though, is the lack of a defined standard underlying the test. This lack has afforded the Department of Commerce discretion in applying the countervailing duty statute. This allows the Department of Commerce to take in consideration the effect and intent of a particular government benefit. While this might be helpful in cases where subsidies serve overwhelmingly important policy objectives it makes countervailing duty investigations opaque and inconstructable.

An alternative to the specificity test would be to abandon the test and lower the de-minimis level. This would transform countervailing duty determinations to a mere mathematical analysis and eliminate Department of
Commerce's discretion. Although this approach would make those determinations more predictable, it disregards that the scrutiny of subsidies only under mathematical aspects neglects economic and political reality. Subsidies serve as an important vehicle for the achievement of policy objectives that have different ranks in different countries. These objectives can reach a far higher rank than the goal to maintain ideal economic conditions.

What has to be changed is the application of the specificity test. A case-by-case approach is reasonable because it takes the intent and effect of a government benefit into account. But the Department of Commerce should establish objective criteria to afford a framework in the determining the thresholds of the dominant use and disproportionate beneficiary analysis. This would make its determinations more understandable and objective and thus more difficult to target.
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