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International Economics
Strategic Analysis For Growth & Development

In collaboration with

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What is a subsidy?

- General definition:
 - A **contribution** by the government
 - Which provides a **benefit** to an individual, business, or institution

Subsidies: role in the trading system and impact

- Reasons for subsidization:
 - Tool for realizing government policies
 - Support or job creation
 - Industrial base support
 - Export promotion
 - A tool to offset market failures and externalities to achieve greater economic efficiency
 - Can be a tool to promote import substitution strategies
 - **Protection to domestic industries** => risk of distortion of the expected competitive relationship resulting from tariff bindings, barrier to trade

The WTO principles: GATT Articles VI and XVI

GATT Articles VI and XVI have been completed by the WTO Agreement on subsidies and countervailing measures (SCM), which is now in practice the legal source for the assessment of subsidies.

WTO Agreement on Subsidies and Countervailing Measures

- Historical introduction to the SCM Agreement
- The SCM Agreement provides rules regulating:
 - the provision of subsidies
 - the use of countervailing measures

WTO Agreement on Subsidies and Countervailing Measures: General Structure

- **Part I** – scope of the Agreement and definitions
- **Parts II and III** – subsidy categories and specific rules and procedures for each category
- **Part IV** – non-actionable subsidies
- **Part V** – substantive and procedural requirements for the imposition of countervailing measures
- **Parts VI and VII** – the institutional structure and notification modalities for the application of the SCM Agreement
- **Part VIII** - rules for various categories of developing country Members
- **Part IX** - transition rules for developed country and former centrally-planned economy Members
- **Parts X and XI** - dispute settlement and final provisions

WTO Agreement on Subsidies and Countervailing Measures

Part I: Coverage

Only a measure which is a “specific subsidy” within the meaning of Part I is subject to multilateral disciplines and can be subject to countervailing measures

- Definition of the term “subsidy”
- Explanation of the concept of “specificity”

WTO SCM Agreement: Part I

Definition
of subsidy

- 1. Financial contribution**
- 2. Benefit**

WTO SCM Agreement: Part I

1. FINANCIAL CONTRIBUTION

- Direct transfer and potential direct transfer of funds
 - grants, loans, equity infusion, loan guarantees
- Government revenue forgone
 - tax credits
- Provision of goods or services or purchase of goods
 - Entrusts or directs private body to carry out one of above
 - *US Export Restraints*
Whether export restraint “entrusts or directs” provision of goods or services
 - *EC – DRAMS Countervailing Measures*
Whether Korean Government had directed private banks to give low-interest loans to Hynix

WTO SCM Agreement: Part I

2. BENEFIT

- Benefit to recipient: market benchmark
- Particular types of financial contribution:
 - **Equity infusion**
Benefit exists if the shares are purchased above their value.
 - **Loan**
Difference between actual rate and commercial rate or if the loan is not otherwise available in the market
 - **Loan guarantee**
difference between interest rate paid and interest rate that would be paid on comparable loan without guarantee
 - **Provision of goods or services**
Price charged is below market price
 - **purchase of services**
Price paid is above “adequate remuneration”, i.e. above market price

WTO SCM Agreement: Part I

SPECIFICITY

- Subsidy **specifically** provided to an enterprise or industry or group of enterprises or industries.
- Rationale: subsidy widely available within an economy => distortion in the allocation of resources presumed not to occur
- Four types of specificity:
 - **Enterprise-specificity:** A government targets a particular company or companies for subsidization;
 - **Industry-specificity:** A government targets a particular sector or sectors for subsidization.
 - **Regional specificity:** A government targets producers in specified parts of its territory for subsidization.
 - **Prohibited subsidies:** A government targets export goods or goods using domestic inputs for subsidization.

WTO SCM Agreement: Part I

3. SPECIFICITY

- De jure specificity
- De facto specificity
 - Limited number of enterprises
 - Predominant use
 - Disproportionate use
 - Manner in which discretion is exercised

Relation between SCM and Agriculture Agreement

- Principle: **all subsidies** are regulated by the SCM Agreement, including agricultural subsidies (Art. 21 of the Agriculture Agreement).
- Agricultural subsidies are however also regulated by the Agreement on Agriculture
- Agriculture Agreement sets upper limits on the amount of permissible domestic and export agricultural subsidies and establishes a mechanism for WTO members to commit to reducing these amounts over time.

Subsidies in the Agriculture Agreement

Scope of application:

- Chapters 1-24 of the Harmonised System of product classification:
 - Chapters 01-05: Animal and animal products
 - Chapters 06-15: Vegetable products
 - Chapters 16-24: Foodstuffs
 - as well as certain (essential) oils, skins and raw textiles
- Fish and fish products are not included, nor are forestry products.

Subsidies in the Agriculture Agreement

Domestic support:

- **Amber Box:** a Global Measurement support is calculated, based on which reduction commitments are taken
- **Green Box (under certain conditions):** these subsidies escape reduction commitments
 - Research, promotion, education, inspection, and other general services
 - Infrastructure services for agricultural areas and rural communities; creation of markets for agricultural products.
 - Public stockholding for food security purposes.
 - Domestic food aid
 - Decoupled income support (i.e. that directly linked to production)
 - Income insurance and safety-net programmes
 - Relief from natural disasters.
 - Structural adjustment assistance provided through producer retirement, resource retirement, and investment aid programmes
 - Payments under environmental programmes.
 - Payments under regional assistance programmes.

Subsidies in the Agriculture Agreement

Domestic support:

- **Blue Box** : direct payments under production restriction plans as long as the following conditions are met : these subsidies also escape reduction commitments.
 - Payments are based on fixed area and yield (subsidy payments for idle fields under the EU Common Agriculture Program)
 - Payments are made on 85% or less of base level of production (the deficient payment system under the US Agriculture Act of 1990(abolished by the US Agriculture Act of 1996).
 - Livestock payments are made on a fixed number of head (incentives for the bovine sector under the EU Common Agriculture Program).

- **Development Box**: these subsidies also escape reduction commitments.

THANK YOU !

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