CHAPTER 7

SUBSIDIES AND COUNTERVAILING MEASURES

OVERVIEW OF RULES

1. BACKGROUND OF RULES

In 1995, as one of the WTO agreements the Agreement on Subsidies and Countervailing Measures (ASCM) came into effect (for details concerning the background to the introduction of the ASCM, see pages 369-370 in the 2017 Report on Compliance by Major Trading Partners with Trade Agreements - WTO, EPA/FTA and IIA -). The ASCM applies to all WTO Members, although there are provisions that provide special and differential treatment for developing countries. The ASCM clarifies the definition of subsidies. It categorizes them into two categories: (1) subsidies that are prohibited on all occasions (the so-called red subsidies -- export subsidies and domestic-content subsidies), and (2) subsidies to specific industries and enterprises against which counteraction can be taken when they adversely affect the interests of other countries (so-called yellow subsidies). The ASCM provides two routes of address subsidies - WTO dispute settlement and imposition of domestic countervailing duties. An outline of the facts and the limitations of the subsidy rules that became apparent after an accumulation of precedents on dispute settlement procedures is given below.

2. LEGAL FRAMEWORK

(1) DEFINITION OF SUBSIDIES

In the ASCM, subsidies are defined as something given (1) by a government or a public body, (2) through a financial contribution, (3) that creates a “benefit” for the recipient company.

The three requisites will be examined in order below, but firstly, “financial contribution” is not limited to “grants” in which governments provide funds to companies without receiving any compensation. It includes tax reduction measures and the provision of items and services. Thus, it has a wider concept than “subsidies” as stipulated in Japanese domestic law (i.e., Subsidy Budget Rationalization Act).

The ASCM is an agreement on goods trade. Therefore, the regulations presume a situation in which benefits from subsidies are provided with respect to goods. Although there may be subsidies that affect service trade (such as government aid to teachers for educational service export), there is at present no regulation of them. Subsidies concerning service trade are currently under negotiations based on Article XV of GATS. Therefore, it is important to firstly ascertain whether subsidies influence goods trade or service trade (or influence both).

(a) “A government or public body” (ASCM Article 1.1(a)(1))

Although a “government” is a concept that includes all governmental organizations, it was not
clear which organizations were “public bodies”. On this point, the Appellate Body determined that in order to be considered a “public body”, the shares of an entity need not only to be owned by a government (in other words, being a government-owned enterprise is not enough), but that entity also needs to possess, exercise or have been delegated some government authority (US-Anti-Dumping and Countervailing Duties (China), DS379 Appellate Body Report, Paragraph 317). Concerning specific applications of this interpretation, in DS379 the Appellate Body found a Chinese state-owned commercial bank to be a “public body” since it exercised government functions in place of the government (US-Anti-Dumping and Countervailing Duties (China) (DS379), Appellate Body Report, Paragraph 356). On the other hand, in DS437 a state-owned company that produces steel was not found as a “public body” because there was no evidence that the company was delegated the right to exercise government functions (United States - Countervailing Duty Measures on Certain Products from China (DS437), Panel Report, para 7.62, 7.75, etc.).

Furthermore, according to this interpretation, while companies that have become temporarily owned by the government for management reconstruction may not be considered as “public bodies”, a company that is judged to have been “delegated government authority” will be considered a “public body” even if the government stock-holding ratio is low.

(b) “Financial Contribution” (ASCM Article 1.1(a)(1) (i) – (iv))

“Financial Contribution” as stated in ASCM is not restricted to grants by the government, but is a concept that includes the active and passive transfer of all types of property, such as renunciation of income (i.e., loans, financing, loan guarantees and tax reductions) and the provision of goods and services.

Although measures that provide goods and services or purchase goods do not constitute “subsidies” under Japanese domestic law (i.e., Subsidy Budget Rationalization Act), for example, if goods and services are purchased by the government at an unsuitable value, that creates an economical effect akin to where the government has provided a grant. Excluding such situations from the provisions of the Agreement on Subsidies naturally might lead to permitting circumvention in which the government could purchase goods at an unsuitable value, aiming to create a same effect as a grant. Therefore, the ASCM considers financial measures from government that have the possibility of creating “benefit” as “financial contribution”. To determine whether a “financial contribution” is actionable under the ASCM requires examining whether it bestows a “benefit” on the recipient.

Moreover, even if a “financial contribution” is provided by a private body, if this was done by entrusts or direction of a government or a public body, it will be treated as a financial contribution from a government or a public body (ASCM Article 1.1(a)(1)(iv)). This provision was put into place to prevent the government from granting subsidies via private bodies in order to evade the regulations of the ASCM. This provision therefore makes instances where the government grants subsidies using private bodies as its “proxy” subject to the ASCM (US-DRAMS Appellate Body report, Paragraphs 113-116). Concerning the definition of entrusts and directs, the Appellate Body considers it difficult to indicate which actions correspond to this. However, it has been determined that administrative guidance by the government may constitute entrustment and direction.

(c) “Benefit” (ASCM Article 1.1(b))

As mentioned above, subsidies in the ASCM are actions that create “benefits” through a “financial contribution”. According to the Appellate Body, a “benefit” is exists when a financial contribution is a more advantageous condition for the recipient when compared with the market
value (Canada-Aircraft, Paragraph 157). In other words, when the government does not receive payment of value equivalent to what would have occurred in a transaction in the commercial marketplace, it would be deemed that there was a “benefit” to the recipient. For example, instances in which the government loans at a rate lower than that of a private financial institution or when the government purchases goods from a company at a price higher than the market price, there will be a “benefit” to the recipient. (Specific case examples are indicated in Article 14 of the ASCM).

In this manner, whether a “benefit” exists or not is determined by comparison with the conditions of market (i.e., market price and interest rates). That being said, there are many cases where it is not clear what the market value is. For example, for loans, the credit capability of the borrower, the prospects of the financing service and the loan amount, as well as the market rates and other circumstances at the time of the loan, need to be considered for the financial organization that does the lending to determine the risk. The conditions of the loans are ultimately determined after negotiating with the borrowing company. In order to determine whether the company that received loans from the government had received a “benefit”, what the market price was needs to be determined. However, it is often unlikely that there exists a company that received loans from a private financial organization that was in the same exact situation as the borrower who received loans from the government. The “market price”, a price that does not exist in reality, needs to be estimated from various situations. Therefore, there has been a tendency for panels and the Appellate Body to seek persuasive evidence (including econometric analysis) that analyzes the circumstances in which the government contributed funds in order to determine what the suitable comparison “market price” should be.

In the case of a new market being created through government intervention, the Appellate Body determined that the government intervention per se does not constitute the granting of “benefits”, i.e. subsidies, and concluded that benefit analysis should be conducted based on the “market value” compared to the government-assisted price or value. More concretely, in the Canada-Ontario case, the Appellate Body did not accept Japan’s claim that “benefits” were assumed to exist in the objectives and structure of the subsidy measure. It held that Japan should specify the “reusable energy market” as a “relevant market” and conduct benefit analysis with consideration to the market value of reusable energy under the previous Renewable Energy Supply system in Ontario. The Appellate Body indicated that, in practice, comparison with the “market value” is required in the determination of “benefits” (Canada-Ontario, Paragraph 5.190).

Furthermore, when it is determined that there is a “benefit” to the recipient of the financial contribution, the benefits from the subsidies are amortized over the products that the recipient produces. If the product in question is a raw material (so-called “upstream products”), there is a possibility that products made from using the raw material (so-called “downstream products”) may have the benefits from subsidies added on as well. Specifically, if benefits from subsidies given to an enterprise that manufactures and sell logs by cutting down timber can be proven to have transferred to softwood which is produced by log processors who use the timber, a subsidized product, the Appellate Body will judge the softwood to be a “subsidized product” as well which could be subjected to countervailing duties. (It is understood that if there is a connection between the log dealer and the log processor, such as the two belong to the same company, the benefits will be naturally transferred. (US–softwood Lumber IV, Paragraphs 155-156)). It should be noted that not only products produced by companies that receive subsidies directly are deemed as “subsidized products”, but also products produced by using subsidized products as their raw material may be deemed as such.
Part II: WTO Rules and Major Cases

(2) Prohibited (RED) Subsidies

Export subsidies and subsidies contingent of the use of domestic products are prohibited for having high trade distortion effects, regardless of whether or not they actually cause adverse effects to other countries. When it is determined that such subsidies are being granted, the ASCM says that the subsidies in question must be abolished without delay (ASCM, Article 4.7).

(a) Export subsidies (ASCM Article 3.1(a))

The Agreement on Subsidies firstly stipulates that the granting and maintenance of “subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance” are prohibited. It then stipulates in a note that “This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.” Due to this provision, it is clear that subsidies that are specified by regulations to be granted only to products that are to be exported will be classified as export subsidies and will be prohibited. However, it was unclear as to what constitutes as export subsidies.

Concerning this point, the Appellate Body indicated that the fact that a grant of subsidies leads to an increase in export volume as a result alone does not make the subsidies export subsidies. However, subsidies that have the characteristic of giving a strong incentive to export sales compared to domestic sales will be judged export subsidies (EC-Large Civil Aircraft, Paragraphs 1045-1056). Furthermore, whether subsidies possess such a characteristic will be judged not by the subjective motive of the government that grants the subsidy but by the objective structure of the subsidy in question (Paragraph 1051).

Subsidies that have been deemed export subsidies by the Panel and the Appellate Body include the following:

- A program in which a public body ensures lower interest terms when a foreign airline company receives fund loans to purchase aircraft from a financial organization (Brazil-Aircraft).
- A tax system in which export goods are sold through an overseas subsidiary whose earnings will receive the privilege of greater tax exemption than earnings earned from domestic sales (US-FSC)
- Subsidies that compensate for the difference to the exporter if the export price falls below the regulated price (US-Upland Cotton)

Assistance to exports by a governmental financial organization (such as when the exporters borrows purchase funds from a financial organization, the exporting country’s government, or public financial organization make loans to the importer or to the financial organization that loans to the importer at a low rate – i.e., “export credit”) will constitute export subsidies due to the characteristic that such loans are granted based on exports. However, export credits granted in accordance with the conditions of the OECD’s “Arrangement of Export Credits” are not considered export subsidies (ASCM Appendix I, Clause (k), Paragraph 2). When a country provides an export credit that deviates from the OECD export credit arrangement, other countries are allowed to provides matching export credits that deviate from the OECD export credit). The Panel in Canada-Aircraft determined that matching export credits do not constitute export subsidies and are excluded from the scope of prohibition by Appendix I, Clause (k), Paragraph 2. (Canada-Aircraft II Paragraph 7.157).
(b) Preferential subsidies for domestic products (ASCM Article 3.1(b))

The ASCM, in addition to prohibiting export subsidies, stipulates the prohibition of granting and maintaining of “subsidies contingent, whether solely or as one of several other conditions upon the use of domestic over imported goods.” This provision exists to sanction in the ASCM subsidies that constitute “violations of national treatment obligations” which are prohibited in the GATT Article III: 4. In other words, subsidies that provide discriminatory treatment depending on whether the parts used for producing products are domestically or foreign produced are “preferential subsidies for domestic products”. Specifically, subsidies that are granted only when domestically produced parts are used or when more subsidies are given when the producer uses domestically produced products rather than foreign-produced products for parts when producing products are “preferential subsidies for domestic products”. Concerning this point, the Appellate Body has determined that subsidies in which the usage of domestically produced products for the production of products is preferentially treated in fact constitutes “preferential subsidies for domestic products”, as well as instances in which such a discriminatory structure is legislatively stipulated (Canada-Autos, Paragraph 143).

Providing subsidies to domestic producers in relation to the production of products itself is not prohibited. Granting subsidies only for domestic producers and not for foreign producers does not constitute “preferential subsidies for domestic products” (Article III: 8(b) of GATT) and is not prohibited by the ASCM. What is prohibited is discrimination between domestic and foreign products concerning parts used for the production of products.

In respect to agricultural products, the Appellate Body has determined that the provisions of ASCM Article 3.1(b) will be applicable since there are no special provisions in the Agreement on Agriculture concerning preferential subsidies for domestic products (US-Upland Cotton, Paragraph 545).

(c) The effect of red subsidies

As mentioned previously, the granting and maintenance of export subsidies and preferential subsidies for domestic products are prohibited (ASCM Article 3.2). If a WTO Member believes that another Member is granting and maintaining prohibited subsidies, the Member can use the dispute settlement procedures. The ASCM provides that disputes related to export subsidies require prompt processing and says they are to be processed in half of the period stipulated in the Dispute Settlement Understanding for other disputes (ASCM Article 4.12). If a Panel or the Appellate Body determines that the subsidies in question constitute export subsidies of preferential subsidies for domestic products, they will recommend the Member to abolish the subsidies in question immediately (ASCM Article 4.7). To be specific, most cases to date have recommended that the subsidy be abolished within three months.

The Member that received the request is obligated to abolish the subsidies. However, it is not clear what constitutes as the “abolition” of subsidies. It is problematic whether promising never again to provide the subsidies that received were determined to be prohibited constitutes “abolishing”, or whether it is returning the already-provided subsidies (and furthermore, if a refund is sought, will it be the entire amount given to the company or will it be restricted to the benefit remaining). The decisions of the Panel and the Appellate Body still are unclear.

The compliance implementation panel in the Australia-leather case addressed this point. Australia, which received subsidy abolition recommendations to abolish a prohibited, claimed that not giving subsidies in the future qualified as “abolition”, while the US claimed that measures do does not qualify as “abolition” unless the benefit remaining with the company that received the subsidy is returned. The Panel did not adopt either of the positions taken by Australia or the US,
and determined that it cannot be said that the subsidy has been abolished unless the entire amount of the subsidy has been returned (Australia–Automotive Leather II (21.5), Paragraph 6.48). However, this decision has been severely criticized by many Members, including Japan. Thereafter, panels and the Appellate Body have not ruled whether subsidies are not “abolished” if they are not returned. Future rulings will be necessary to determine whether the refund of subsidies by the company is necessary in order to satisfy a subsidy “abolition” recommendation (and if the refund is necessary, its scope), and what “abolition” signifies.

(d) Countermeasures for WTO recommendation non-compliance

If a WTO recommendation that seeks the abolition of subsidies has not been complied with, the complainant member can seek authorization to take an appropriate countermeasure (i.e., increasing tariffs) (ASCM, Article 4.10). The meaning of what “appropriate” means is referred to in the footnote to the Article as “This expression is not meant to allow countermeasures that are disproportionate in light of the fact that the subsidies dealt with under these provisions are prohibited”.

This provision is a “special provision” of DSU Article 22.4, which requires that countermeasures be “equivalent to the level of the nullification or impairment” in cases of WTO noncompliance with WTO recommendations. In other words, in disputes related to Agreement violations other than subsidies, the fact that the interest of the complainant country has been “nullified or impairment” is a requirement for receiving WTO authorization to take countermeasures (GATT Article XXIII). Furthermore, the nullification and impairment of the benefit of the complainant country will be estimated based on DSU Article 3.8. The responding country has the responsibility to refute). In contrast to this, export subsidies and preferential subsidies for domestic products are required to be abolished based only on the fact that they have the characteristics of corresponding to that type of subsidies. Therefore, the complainant country is not required to prove whether there was any effect of “nullification or impairment”. The level of “nullification or impairment” is not relevant for export subsidies and preferential subsidies for domestic products. Instead, a countermeasure that is of an “appropriate” degree is accepted.

To be specific, the total amount of red subsidies given by the government has been approved as the upper limit of “appropriate countermeasure” in many cases. That being said, there have been cases where an amount that was 20% greater was the estimated amount of countermeasures since a higher degree of countermeasure is necessary in order to fulfill the requirement of prompt compliance with the WTO recommendation (Canada–Aircraft II (22.6), Paragraph 3.121). In such a manner, the upper limit of the countermeasures for noncompliance with abolition recommendation of red subsidies is an amount that the arbitrator believes to be “appropriate”. It could be said that the discretion of the arbitrator is acknowledged with respect to this decision. Therefore, the upper limit cannot be predicted with any certainty, though likely it will be higher in amount compared to countermeasures for violations of Agreements other than the ASCM.

(3) Actionable (yellow) Subsidies

Even if the subsidies do not constitute export subsidies or preferential subsidies for domestic products, subsidies with “specificity” that cause adverse effects to other countries may be required as a result of WTO dispute settlement to be abolished or removed. Therefore, the concept of “specificity” and what situations constitute “adverse effect” become issues to consider.

(a) Specificity

In ASCM Article 21, the “principles” for determining the existence of specificity are stipulated:
Chapter 7: Subsidies and Countervailing Measures

(a) if the granting authority explicitly limits access to a subsidy to certain enterprises, then such subsidy shall be specificity; (b) if the grant recipient or its amount is stipulated by an objective criteria/condition, then there is no specificity; and (c) although it is considered that there is no specificity according to (a) or (b), if subsidies can be deemed to be used in fact by a specific company/industry, then there is specificity.

Considering the principles mentioned above, the Appellate Body states that (a) and (b) are both provisions concerning the recipient’s qualification for receipt of subsidies and that the factors of both provisions should be examined in determining the existence of specificity (US–AD/CVD (China,) Paragraph 368). If (a) and (b) are looked at from the perspective that they are provisions concerning the recipient’s qualification, subsidies in which different types of industries can receive the assistance do not have specificity, while subsidies in which only a specific industry (in other words, subsidies which only certain companies/industries are not eligible to receive) have specificity. In other words, subsidies that stipulate certain criteria and conditions as a requirement for the granting of subsidies (i.e., revenue, earnings condition and number of employees) can be granted to any type of business as long as the criteria and conditions of “specificity” are not met. However, subsidies that only approve the application of certain companies/industries mean that there obviously exist companies/industries that are excluded from being recipients of the government assistance. The former is judged not to have specificity, while the latter is judged to be specific.

That being said, even among subsidies that all types of companies/industries can receive, there are in fact those that only specific companies/industries can receive (or do not receive). (c) stipulates that in such situations, there is “specificity”. For example, even if revenue, earning conditions and the number of employees are the objective criteria/conditions, if there is only one company that fulfills such criteria/conditions in fact, only this one company receives those subsidies; this is no different than specifying the recipient’s qualification for the company in question. Therefore, it will be judged that there is specificity.

Additionally, export subsidies or preferential subsidies for domestic products are both deemed to be subsidies with specificity (ASCM Article 2.3). Therefore, there is no need to examine for above-mentioned specificity; red subsidies automatically will be treated as “subsidies with specificity” and will be subject to countervailing duties as mentioned later on.

(b) Adverse effects

ASCM Article 5 stipulates three types of adverse effect: (1) injury to domestic industry, (2) nullification and impairment of benefits given based on the GATT (in particular the benefit of tariff concession), and (3) serious injury.

(1) Injury to domestic industry is a concept that is also a requirement for anti-dumping and countervailing duties. Detailed provisions for the determination of injury are stipulated in the ASCM Article 15. Moreover, the remedy based on this provision (the imposition of countermeasures based on a WTO recommendation) has the same effect as countervailing duties in the sense that it prevents injury occurring to domestic industries. Therefore, Members cannot impose countermeasures based on a WTO recommendation and countervailing duties at the same time (note to ASCM Article 5).

(2) Nullification and impairment of benefits given based on the GATT (in particular the benefits of tariff concession), is stipulated as having the same meaning as Article XXIII: I of GATT. That being said, in order to satisfy the requirements, it is necessary that (a) the negotiating party could not have predicted during the tariff negotiation that the subsidy in question would have been implemented, and (b) due to the subsidy in question, the competitive position of imported goods
would be lowered (EC-Can, Paragraph 55). That being said, for the requirements for (b), it is believed that it is possible to prove that there was “serious injury” (or threat of it) as import substitutes have been introduced into the market (or there is a threat that they will be) as mentioned later on. Therefore, it seems unnecessary to include the nullification and impairment of benefit of a specific tariff negotiation. In fact, there are almost no cases where such claims have been made.

(3) Serious injury is stipulated in Article XVI: I of GATT. However, since the details were not clear, it was expanded in the “Subsidies Code” during the Tokyo Round. The ASCM further expanded the definition and explanation in the “Tokyo Code”. ASCM Article 6.3 stipulates that serious injury is generated if the effect of subsidies is to: (a) displace or impede the import of a like product of another Member into the market of the subsidizing Member; (b) displace or impede the export of a like product of another Member from a third-country market; (c) cause significant price undercutting or price suppression, price depression or lost sales by reason of the subsidized product as compared with the price of a like product of another Member in the same market; or (d) increase the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years, and this increase follows a consist trend over a period when subsidies have been granted. Countervailing duties cannot resolve these phenomena. Therefore, there is a tendency for WTO dispute settlement procedures to be used where the adverse effect is experienced in a market other than the domestic market of the complainant Member. There have been disputes over the existence of the “serious injury” regarding products such as cotton and civil large aircraft that have such tendencies.

In order to claim that a subsidy has caused “serious injury”, there needs to be a causal link between the effect of subsidies and “serious injury”. Concerning the causal link, the Appellate Body has ruled that conditional relationships that state that “but for” are not enough; a “genuine and substantial relationship” is necessary (US-Upland Cotton, Paragraph 438). Therefore, in situations where the relationship between the effect and the cause is thin, such as claiming “one thing has led to another”, even if the subsidy was a factor that caused the result, pursuant to the ASCM the subsidy cannot be acknowledged to have caused “serious injury”.

Furthermore, since countervailing duties, which will be mentioned later are intended to counteract the effect of subsidies, the size of benefit needs to be accurately calculated. However, the Appellate Body has ruled that when determining the causal link between subsidies and “serious injury”, there is no need for them to be accurately calculated based on the benefit of the subsidies (US-Upland Cotton, Paragraph 465). Based on this, panels have indicated that it is important to consider the nature of subsidies when determining such causal links. From such determinations, one can see that panels and the Appellate Body tend to determine that a qualitative analysis is necessary when determining causal links.

Since the ASCM came into effect, subsidies that panels and the Appellate Body determined to cause “serious injury” include the following:

The exemption of domestic taxes which are only approved when domestic products are used at a fixed ratio (Indonesia-Automobile Panel. The subsidies in question constituted preferential subsidies for domestic products. However, due to the ASCM Article 27.3, Indonesia at that time was not covered by ASCM Article 3.1(b).

Subsidies in which the amount varies in conjunction with market price (Appellate Body in US-Upland Cotton) – in which it was judged to have significantly increased the price of like products in the global market.

A subsidy which provides a low-rate loan for the construction of a new type of civil aircraft. If
the completed new type of aircraft did not reach its sales targets, then the repayment obligations would be absolved (so-called “launch aid”). In Appellate Body report in EC-Large Civil Aircraft it was determined to have caused displacement of imports within the EC regional market and displacement of import and lost sales of like products in a third-country market. Provision of funds and facilities from the American government for developing a new type of civil aircraft.

Tax reduction measures that were linked to the sales of aircraft (US–Large Civil Aircraft). It was determined that it caused a displacement of imports, lost sales, and price suppression of like products in a third-party country.

All subsidies that have been determined to have caused “serious injury” in the past could have been said to have had the objective of directly decreasing the price of the product. In other words, these subsidies aimed to maintain and strengthen competitiveness in markets by giving an “inflation” called subsidies. Therefore, as soon as the “inflation” is removed, the competitiveness of the products in question will be lost as well. In light of the spirit of the ASCM, which tries to avoid elimination of the international competitiveness of products because of the size of subsidies that other country’s grant, it is necessary to restrict the granting of subsidies with natures mentioned above. On the other hand, subsidies that are necessary to correct mistakes of the market (for example, subsidies with the objective of environmental protection or subsidies for adjusting industrial structures) do not aim to maintain or strengthen competitiveness in markets by giving an “inflation”; rather, they have the characteristic of promoting international competitiveness that should exist. Therefore, such subsidies should not be considered the same as subsidies that aim to directly lower the price of products.

(Addendum) Presumptive provision of serious injury

ASCM Article 6.1 stipulates that if a subsidy satisfies certain quantitative or qualitative requirements, it will be presumed to have “serious injury”. Unless the country that is granting the subsidy proves that there has been no serious injury it will be considered that serious injury by the subsidy exists (ASCM Articles 6.2 and 6.3).

However, since these provisions lost their effect five years after the Agreement came into effect (ASCM Article 31), countries that have requested the establishment of a panel need to prove serious injury as stipulated in the ASCM Article 6.3.

(c) The effect of yellow subsidies

Governments that have subsidies that have specificity and that cause adverse effects must either take appropriate measures to remove the adverse effect of the subsidies or be withdraw them (ASCM Article 7.8). If a WTO Member believes that another Member is granting and maintaining such subsidies, it can use the dispute settlement procedures. If the Panel or the Appellate Body determines that the subsidy in question possesses specificity and causes adverse effects to the complainant Member, they will be requested to act appropriately to remove the adverse effects caused by the subsidies within six months or to withdraw it.

That being said, as mentioned earlier, it is not clear what constitutes “withdrawal” of a subsidy. Furthermore, it is not clear what specific measures are “appropriate measures for removing adverse effects”. Clarification by precedent is needed at this point.

(d) Countermeasures for noncompliance with WTO recommendations

If WTO recommendations were not complied with, the complainant Member can take countermeasures (i.e., increasing tariffs) commensurate with the degree and the nature of the adverse effects that have been determined to exist (ASCM Article 7.9). It is not clear how this
provision differs from DSU Article 22.4, which stipulates that countermeasures should be equal “to the level of the nullification or impairment”.

To date, the US-Cotton case is the only case in which a decision was made concerning a countermeasure based on the WTO recommendation regarding a yellow subsidy. The arbitrator used the adverse effect that Brazil, the complainant country, received (specifically, the decline in sales of cotton that was actually sold and the inability to sell cotton that it should have been able to sell), as a basis for calculation. The arbitrator calculated the amount by comparing the situation as if there was no subsidy with the actual situation, and determined that amount as the amount of countermeasure that was “commensurate with the degree and the nature of adverse effects”.

In respect to the losses incurred by a complainant Member, this approach calculating the level of the countermeasure as the difference between reality and a “situation in which a WTO Agreement violation did not occur” seems to be no different than DSU Article 22.4, which stipulates that it “shall be equivalent to the level of the nullification or impairment”. Whether the calculation of countermeasures of yellow subsidies differs substantially from the countermeasures related to a WTO Agreement violation will become clear from an accumulation of precedents.

(4) COUNTERVAILING DUTIES

(a) Outline

As mentioned previously, depending on the subsidy, it may decrease the price of the product as a result of the benefit from the subsidy. Thus, it provides a competitive disadvantage to the products of importing country that does not grant subsidies. Therefore, Article VI of GATT approves Members imposing countervailing duties, special taxation for protecting domestic industries from subsidies, and the ASCM has detailed provisions on the procedure for countervailing duty subjection.

(b) Actionable Subsidies

Subsidies that become subjects of countervailing duties are “subsidies with specificity”. The definitions of “specificity” and “subsidies” are as mentioned above. Since export subsidies and preferential subsidies for domestic products are both deemed to be specific (ASCM Article 2.3), these subsidies can become subject to countervailing duties. On the other hand, countervailing duties cannot be imposed for subsidies without any specificity even if they cause losses for the domestic industries of the importing country. Furthermore, it should be noted that there are cases where the triggering of countervailing duties becomes restricted even for subsidies with specificity.

Firstly, if countervailing duties and anti-dumping duties for export subsidies compensate for the same situation, they cannot be imposed at the same time (Article VI: 5 of GATT). Due to the characteristics of export subsidies treating export sales more advantageously than domestic sales, they create a situation in which export prices are lower than domestic sales prices. If such a situation occurs, this simultaneously satisfies the requirement of imposing an anti-dumping duty, which is “when the export price is lower than the domestic sales price”. In such situations, where the imposition requirements of anti-dumping duties have been satisfied by an export subsidy, if countervailing duties and anti-dumping duties are imposed simultaneously, it will cause a “double remedy”. Therefore, in such situations, it is enough to trigger either anti-dumping duties or countervailing duties, with simultaneous imposition being prohibited. On the other hand, the simultaneous imposition of anti-dumping duties and countervailing duties for separate reasons is not prohibited.

Secondly, when imposing a countermeasure against WTO recommendations based on adverse
effects to domestic industries, countervailing duties for the same subsidy cannot be imposed (Footnote to ASCM Article 5). Since countervailing duties and WTO dispute both are systems for protecting domestic industries from loss, there is no necessity to simultaneously conduct both remedy procedures for the same objective. On the other hand, the simultaneous imposition of countervailing duties cannot be prevented if the displacement of imports, or price suppression etc. within the country granting subsidies and the third-country market, are decided in WTO dispute settlement proceedings.

(c) Injury to Domestic Industry and Causal Link

These provisions are stipulated in detail in ASCM Articles 15 and 16, with their content being virtually the same as the provisions of the AD Agreement (see Chapter 5 Anti-Dumping Measures).

(d) Effects

Where it is determined that the injury to domestic industries is occurring as a result of subsidies with specificity, the importing country can impose subject countervailing duties in the excess of the amount of subsidy found to exist on the product in question (ASCM Article 19. 4). The amount of subsidies is the difference between the financial contribution at issue and the situation if a similar financial contribution was given in the marketplace (in other words, the amount of benefit created by the financial contribution) (ASCM Article 14). Since the objective of countervailing duties is to prevent domestic products from becoming competitively disadvantaged due to imported goods having the benefits of subsidies, this amount is set as the upper limit for countervailing duties in order to align the competitive conditions of imported goods and domestic goods by setting the tariffs to the amount of the benefit of subsidies.

If a subsidy of the same amount is granted every year, countervailing duties can correspondingly counteract the upper limit to the amount of subsidy every year. However, if capital investments and such have been provided as one-time only subsidies (i.e., financing and loans), how to calculate the “benefit of subsidies” and imposes countervailing duties becomes problematic. Although there are no related provisions in the Agreement on Subsidies, the investigating authority of the importing country should determine logically how the benefit of subsidies is used over the course of years and how it should be amortized. Concerning this point, if the investigating authority determines that the benefit of subsidies of financing and loan exemption have been allocated over five years, the Appellate Body has stated that countervailing duties cannot be imposed from the sixth year onward (Japan-DRAMS Appellate Body report, Paragraph 214).

(Addendum) Non-actionable (green) subsidies

ASCM Articles 8 and 9 state that certain subsidies with the objective of research and development, regional development assistance and environmental protection do not constitute “yellow subsidies”, even if they are determined to have specificity. Therefore, they were stipulated to be “non-actionable” and subject to WTO dispute settlement or countervailing duties. However, this provision sunsetted five years after the effective date of the WTO (ASCM Article 31). Therefore, currently, they have become “yellow subsidies”, and are the subject to imposition of countervailing duties.

3. SPECIAL PROVISIONS FOR DEVELOPING COUNTRIES

(1) SPECIAL PROVISIONS FOR EXPORT SUBSIDIES

Although Article 3.1(a) of the ASCM prohibits export subsidies, Article 27.2(a) exempts member countries defined in Annex VII(b). Of Member countries listed in Annex VII(b), some were
excluded from the list following the establishment of the implementation requirements of Annex VII(b) under Paragraph 10.1 of the Doha Ministerial Declaration, and 14 countries qualified for the exemption at the end of 2017 (see Figure II-7).

Exemptions regarding export subsidies under Article 27.2(b) of the ASCM reached the time limits for expiration at the end of 2015. Member countries granted the exemptions were required to abolish all export subsidies by the end of 2015, after the final two-year phase-out period, and their notifications will be reviewed in the future. For more details concerning the background, see pages 380-381 in the 2017 Report on Compliance by Major Trading Partners with Trade Agreements - WTO, EPA/FTA and IIA -.

(2) Special provision concerning WTO consultation requests regarding “yellow subsidies”

ASCM Article 27.9 stipulates that WTO dispute settlement action “yellow” subsidies can be taken against developing countries only where there is nullification or impairment or injury to the domestic industry of the exporting country caused by displacement or impedance of its products within the developing country that is providing subsidies.

Figure II-7-1 Members with export subsidies under Annex VII(b) (12 countries)

Bolivia, Cameroon, Congo, Cote d’Ivoire, Ghana, Honduras, Kenya, Nicaragua, Nigeria, Pakistan, Senegal and Zimbabwe.

(Note 2) The Dominican Republic, Guatemala and Morocco were removed from Annex VII(b) in 2003, and Egypt and the Philippines were removed in 2011 based on the provisions of Annex VII(b). (G/SCM/110) (G/SCM/110/Add.14)

4. Countervailing measures

There were only two cases that were investigated in Japan, including one initiated before the inauguration of the WTO. Of these, only one case resulted in duty imposition.

Japan has not been subject to an investigation by another country in recent years. However, countervailing duties are frequently imposed in the world, and the number of countervailing measures implemented in recent years is higher compared with the past (see Figure II-7-4).

Figure II-7-2 Number of Countervailing Duty Investigations on Major Countries Since WTO’s Inception (As of the end of 2016)

---

1 Japan initiated an investigation on imports of cotton thread from Pakistan in April 1983, but did not impose a countervailing duty because Pakistan eliminated the subsidy in February 1984. An application requesting a countervailing duty against Brazilian ferro-silicon was filed in March 1984, but was withdrawn in June of that year and an investigation was never initiated.
Part II: WTO Rules and Major Cases

Exemptions regarding export subsidies under Article 27.2(b) of the ASCM reached the time limits for expiration at the end of 2015. Member countries granted the exemptions were required to abolish all export subsidies by the end of 2015, after the final two-year phase-out period, and their notifications will be reviewed in the future. For more details concerning the background, see pages 380-381 in the 2017 Report on Compliance by Major Trading Partners with Trade Agreements - WTO, EPA/FTA and IIAs -.

(2) SPECIAL PROVISION CONCERNING WTO CONSULTATION REQUESTS REGARDING "YELLOW SUBSIDIES"

ASCM Article 27.9 stipulates that WTO dispute settlement action "yellow" subsidies can be taken against developing countries only where there is nullification or impairment or injury to the domestic industry of the exporting country caused by displacement or impedance of its products within the developing country that is providing subsidies.

Figure II-7-1 Members with export subsidies under Annex VII(b) (12 countries)
Bolivia, Cameroon, Congo, Cote d'Ivoire, Ghana, Honduras, Kenya, Nicaragua, Nigeria, Pakistan, Senegal and Zimbabwe.

(Note 2) The Dominican Republic, Guatemala and Morocco were removed from Annex VII(b) in 2003, and Egypt and the Philippines were removed in 2011 based on the provisions of Annex VII(b). (G/SCM/110) (G/SCM/110/Add.14)

4. COUNTERVAILING MEASURES

There were only two cases that were investigated in Japan, including one initiated before the inauguration of the WTO. Of these, only one case resulted in duty imposition.

Japan has not been subject to an investigation by another country in recent years. However, countervailing duties are frequently imposed in the world, and the number of countervailing measures implemented in recent years is higher compared with the past (see Figure II-7-4).

Figure II-7-2 Number of Countervailing Duty Investigations on Major Countries Since WTO's Inception (As of the end of 2016)

5. ECONOMIC ASPECTS AND SIGNIFICANCE

Subsidies have economic effects on domestic industries and trades. For details regarding subsidies' effects on competition conditions, see page 384 in the 2017 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-.

6. NEGOTIATIONS IN THE DOHA ROUND

(1) BACKGROUND OF DISCUSSIONS

(Please see pages 433-434 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

(2) GENERAL REGULATIONS ON SUBSIDIES AND COUNTERVAILING MEASURES

For general subsidies, revision of the related provisions and revival of the provisions that expired in the past was proposed based on decisions of the panel and Appellate Body to date. In February 2006, the United States proposed funding of companies with bad financial situations, industrial restructuring, subsidies that inhibit rationalization and the currently expired Article 6.1 as new candidates for the category of prohibited subsidies. In June 2007, the United States submitted a proposal for amendments of the agreement provisions. Also, in May 2006, it submitted a proposal regarding the distribution of subsidy profits.

In May 2006, the EU proposed that dual pricing systems for export and domestic sales and below cost investment should be added to the category of prohibited subsidies.

In May 2006, with regard to "significant harm" Canada proposed revival of Article 6.1 (expired...
in 1999) and improvements in the discipline. In the same month, Brazil also made a proposal regarding "significant harm". Canada submitted proposals on regarding "the transfer of subsidy profits" in April 2004 and on “significance” in May 2006, stating that various elements should be comprehensively considered.

Australia, since April 2004, has made four proposals on the clarification of abolishing subsidies on established WTO violations and four on the clarification of “Export Subsidies De Facto”; in November 2005, a proposal was also made by Brazil.

In addition, provisions on export confidence (Brazil) and clarification on countervailing duty rules (Canada, EU, Taiwan, India) were proposed and discussions were held.

Developing countries have requested Special and Differential Treatment (S&D), and in May 2006, India, Egypt, Kenya and Pakistan submitted a proposal related to criteria for exemption of export subsidies.

Proposals were made in December 2009 by China on the (1) treatment of subsidies that are discovered after the investigation and (2) expansion of consultation procedures before the start of a countervailing duty investigation. In October 2010, China submitted a proposal regarding Facts Available related to the countervailing duty investigation procedure, and India submitted a proposal on related issues.

In June 2015, the EU proposed enhancing transparency in the notification obligations, and in October of the same year, Russia also proposed increasing transparency in processes such as the disclosure of essential facts and handling of confidential information concerning the countervailing duty investigation procedure.

Meanwhile, developing countries requested Special and Differential Treatment (S&D) once again, and made proposals such as excluding subsidies for regional development and technology development, etc. from the dispute settlement and excluding developing countries’ subsidies from the category of subsidies contingent upon the use of domestic goods over imported goods.

Although Japan did not submit any proposal papers, it is in favor of the clarification and reinforcement of subsidy/countervailing measures in the negotiations, as with reinforcing AD discipline.

(3) Fisheries Subsidies

With regard to the Chairperson's text, many countries including Japan submitted proposal papers and actively discussed clarification and improvement of the discipline of fisheries subsidies. New Zealand, Chile, and the United States etc., (Friends of Fish) are of the opinion that fisheries subsidies not only distort the market but also trigger the deterioration of marine resources, and so fisheries subsidies should be prohibited in general, and only in exceptional cases should they be permitted. In response, Japan, the Republic of Korea, Taiwan and the EU, etc., opposed, stating that prohibition of fisheries subsidies not only has the risk of prohibiting subsidies contributing to resource management, but also violates the Doha Declaration, which calls for seeking clarification and improvements in the fisheries subsidy discipline in line with the principles of the WTO Agreement on Subsidies, and the Hong Kong Ministerial Declaration, which opined that only fishery subsidies that adversely affect the natural resources should be banned. At the same time, many developing countries stated that disciplines should not be strengthened in a manner that hampered the development of fisheries in developing countries in any form. Discussions were held based on various positions.

Although the negotiations had been stalled since 2011, in 2015, several countries began to
submit proposals from new viewpoints, such as developing disciplines with a narrower scope of prohibited subsidies and enhancing transparency, and to hold discussions. While fisheries subsidies will continue to be discussed in the future, Japan will participate in the discussions based on a position that only fisheries subsidies that truly have an adverse effect on resources should be prohibited.

---

**MAJOR CASES**

1. **COUNTERVAILING MEASURES BY THE UNITED STATES AND EU ON KOREAN DRAMS (DS296, 299)**

   (Please see pages 436-437 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

2. **COUNTERVAILING MEASURES BY JAPAN ON KOREAN DRAMS (DS336)**

   (Please see pages 437-438 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

3. **EU AND REPUBLIC OF KOREA DISPUTES ON SHIPBUILDING (DS273, DS301)**

   (Please see page 438 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

4. **EU AND UNITED STATES – MEASURES AFFECTING TRADE IN LARGE CIVIL AIRCRAFT (DS316/347, DS317/353/487)**

   (1) **BACKGROUND**

   In the late 1980s, European Airbus S.A. drastically increased its share of the civil aircraft market through the use of subsidies from many governments in the EU (the UK, France, Germany and Spain). In response, in May 1991, the US requested consultations under the Tokyo Round Subsidies Agreement with the then-EEC. The US claimed that the EU’s aircraft subsidies were inconsistent with their obligations under the GATT Subsidies Agreement. In July 1992, the US and the EU signed the 1992 US-EU Agreement on Trade in Large Civil Aircraft, which included a prohibition of future production support and a limitation on the share of government support for the development of new aircraft programs to 33 percent of the project’s total development cost. The US withdrew its request for consultations.

   However, responding to the fact that Airbus sold more large civil aircraft than Boeing in 2003, the US once again alleged that “launch-aid” and other forms of support by the EU and its member States to Airbus were inconsistent with the 1992 Agreement and the ASCM. On October 6, 2004, the US requested WTO consultations with the EU and with the Member States in WTO dispute settlement procedures (DS316) concerning measures affecting trade in large civil aircraft, and also notified its intention to repeal the 1992 Agreement, claiming that the EU’s subsidies were in violation of the Agreement. At the same time, the EU requested WTO consultations with the US, claiming that the US’s support for large civil aircraft violated the ASCM (DS317). The EU also rejected the US’s unilateral abrogation of the EU-US 1992 Agreement.
Part II: WTO Rules and Major Cases

Then, on January 11, 2005, the US and the EU suspended the WTO dispute procedure and began negotiations toward a new bilateral agreement. However, the negotiations broke down on June 13, 2005, and both sides requested establishment of WTO dispute settlement panels. On July 20, 2005, the DSB established panels, and Japan, Australia, Brazil, Canada, China and Republic of Korea participated as third parties.

(2) AIRBUS CASE (DS316, DS347²)

The DS316 panel report was issued on June 30, 2010. The panel found that the “launch aid” provided by governments in the EU to Airbus are export subsidies, and “serious prejudice” was being caused to interests of the other Member because Airbus products that received subsidies from governments in the EU were replacing or impeding the export and import of like products made by Boeing. The EU appealed on July 21, 2010, and Appellate Body hearings were held in November and December 2010. (As of Jan 24, 2011, the Appellate Body report had not been issued.) The DS353 panel report also has not yet been issued.

On May 18, 2011, the DS316 Appellate Body report was issued. The Appellate Body overturned the decision by the Panel that the low-interest loans provided by several EU member state governments to Airbus called “Launch Aid”, in which the reimbursement was exempted depending on the sales of aircraft, constituted export subsidies. The Appellate Body decided that the subsidies in question did not satisfy the provisions on export contingency; however, it determined such loans caused significant adverse effects on the US industry.

Within this report, the Appellate Body determined that the appealing country does not need to prove that the adverse effects continue to exist at the time of the dispute settlement proceeding. Therefore, the Appellate Body rejected the claim by the EU that the benefit of the subsidies had disappeared at the time the adverse effects had existed. Upon receiving this decision, on December 1, 2011, the EU reported that they had complied with the recommendation by the Appellate Body. However, the US requested bilateral consultation with the EU and submitted an application for countermeasures prior to establishment of the DSU Article 21.5 Compliance Panel on the 9th of the same month, claiming that the US had doubts about the EU assertion. The EU objected to the amount of the US countermeasure application and the decision of the amount of countermeasures was referred to WTO arbitration. On January 12, 2012, an agreement was established to conduct the bilateral consultation before the arbitration procedure to determine the amount of countermeasures. On March 30, 2012, the US requested establishment of a compliance panel and the panel was set up on April 17 of the same year. A panel meeting was held in April 2013. On March 30, 2012, the US requested establishment of a compliance panel and the panel was set up on April 17 of the same year. A panel meeting was held in April 2013. In September, 2016, the compliance panel circulated its report. It denied the US argument that EU subsidies are export subsidies and local content subsidies. The U.S. also argued that measures to “remove the adverse effect” of the subsidies or “withdraw them” (Article 7.8) had been taken with respect to yellow subsidies, and the panel found that the EU had not complied with the recommendations. In October 2016, the EU appealed and the US cross-appealed these panel determinations. The Appellate Body meetings were held in May and September 2017.

(3)BOEING CASE (DS317, DS353)

The EU made a request for consultations in order to cover broader topics than what was

² In addition to DS316, on January 31, 2006 the US requested new consultations on subsidies from the Government of Wales in the UK to Airbus UK and an additional panel (DS347) was established on April 10, 2006. However, suspension of DS347 until completion of the panel examination of DS316 resulted in its abolition after 12 months on October 7, 2007.
discussed in the DS317 panel. Based on this request, an additional panel (DS353) was established on February 17 of the same year (the procedures for DS317 were suspended).

Concerning DS353, the Appellate Body issued a report on March 13, 2012. It supported the Panel’s decision that research and development subsidies that the American government (i.e., NASA and the Department of Defense) granted caused “significant harm” to the EU. In response to this, on September 23, 2012, the US sent the DSB a report on implementation of the DSB recommendations, but on October 11, the EU expressed doubts and requested the establishment of a compliance panel; on 30th of the same month, a panel was set up. Furthermore, prior to the request for panel establishment, the EU filed an application of countermeasures on September 27, 2012, and as a result of subsequent consultations with the United States, the arbitration process for the countermeasures was temporarily suspended. Subsequently, a panel meeting was held in October 2013 and deliberations are ongoing.

The EU made a new request for consultations on the preferential taxation measures for aerospace companies, etc. by the State of Washington in December 2014, and a panel was established in April 2015 (DS487). Subsequently, a panel meeting was held in October 2013. The panel circulated a report in June 2017, which stated that the United States failed to appropriately comply with the Appellate Body recommendation to eliminate the “significant harm” caused by said research and development subsidies. Dissatisfied with part of the panel’s finding concerning damage, the EU appealed and the United States cross-appealed these panel determinations in June of the same year.

(4) Boeing Case II (DS487)

The EU made a new request for consultations on the preferential taxation measures for aerospace companies, etc. by the State of Washington in December 2014, and a panel was established in April 2015 (DS487). The panel report was circulated in November 2016. The report pointed out that the state’s preferential taxation measures, which were applied to companies that had final assembly establishments, etc. for aircrafts in the State of Washington, were substantially local content subsidies and thus constituted a violation of the law. In December 2016, the U.S. appealed.

In September 2017, the Appellate Body circulated a report. The Appellate Body overruled the panel’s decision, finding that the provision in question merely required companies to have assembly establishments in the State of Washington and did not require the use of domestic products (the program allowed the use of imported components as well). With this decision, the United States’ reversal became final.

5. United States and Canada – Dispute on Softwood Lumber (DS236, DS257, DS264, DS277)

Most of Canada's forests are owned by the provincial or federal governments and the provinces administer tenure systems (known as the “stumpage program”) which provide harvesting rights for standing timber on provincial lands to the provincial lumber industry.

On May 22, 2002, the US International Trade Commission (USITC) made a final determination that a US industry was threatened with material injury. Subsequently, the US government imposed a countervailing duty of 18.79% (flat rate) and an average anti-dumping duty of 8.43% (set by company).

The Canadian Government claimed that the countervailing duties imposed by the United States violated the WTO Agreements. Upon the request of the Canadian Government, a WTO panel was established regarding the provisional determination on December 5, 2001 (DS236), and another panel to examine the final determination on October 1, 2002 (DS257). With respect to the
Part II: WTO Rules and Major Cases

provisional determination (DS236), the panel circulated its final report on September 27, 2002, finding that: (1) the Stumpage Program constituted subsidies defined under the ASCM; but (2) the US investigation violated the ASCM. The report was adopted at a special meeting of the DSB on November 1, 2002.

On August 29, 2003, the Panel with respect to the final determination (DS257) circulated its report including the same findings as DS236. However, the US government appealed the report to the Appellate Body on October 21, 2003. On January 19, 2004, the Appellate Body circulated its report reversing the finding of the panel report that the US method to calculate the subsidies violated the ASCM and upholding the finding that the US “pass through” analysis violated the ASCM. The Appellate Body report was adopted at a regular meeting of the DSB on February 17, 2004. On December 16, 2004, the DOC issued a revised countervailing duty determination, and then it published the final results of the first administrative review on December 20. Canada again claimed that these measures violated the WTO Agreements and requested the establishment of a WTO compliance panel under Article 21.5 of the DSU. The compliance panel was established on January 14, 2005. The panel report was issued on August 1 and the Appellate Body report was circulated on December 5, finding that these measures were, again, inconsistent with the WTO Agreements.

In addition, another panel was established at the Canadian Government’s request on January 8, 2003 (DS264), to examine the final US Antidumping determination on Softwood Lumber from Canada. The panel report was issued on April 13, 2004; following an appeal, the Appellate Body issued its report on August 11, 2004, finding that the final antidumping determination was inconsistent with the WTO Anti-Dumping Agreement in determining the existence of margins of dumping on the basis of a “zeroing” methodology. These reports were adopted on August 31, 2004. Although the DOC issued a revised antidumping determination on April 15, 2005, Canada requested a compliance panel under DSU 21.5, claiming that the measure still violated the WTO Agreement and did not comply with the recommendations and rulings. As a result, a Compliance Panel was established on June 1, 2005. On April 3, 2006, the panel report was issued describing the US measures as being consistent with the WTO and as complying with recommendations and rulings under the DSU, and Canada appealed to the Appellate Body. On August 15, 2006, the Appellate Body reversed the panel’s conclusion, distributed a report saying that the US measures were a violation of the WTO Agreements, and did not comply with the recommendation and rulings of the Appellate Body report.

Furthermore, a WTO panel was established on May 7, 2003 (DS277) to examine the USITC’s injury determination. The panel found that the USITC’s analysis violated WTO Anti-Dumping and ASCM Agreements. The panel report was circulated on March 22, 2004, and adopted on April 26, 2004, at a regular meeting of the Dispute Settlement Body. The USITC made a revised determination on November 24, 2004, but Canada again objected to this measure and a DSU 21.5 compliance panel was established on February 25, 2005. On November 15, the compliance panel issued its report, concluding that the USITC determination was consistent with the WTO Agreements. Canada appealed to the Appellate Body, and on April 13, 2006, the Appellate Body distributed a report finding that the revised decision by the USITC was a violation of the WTO Agreement and overturning the panel’s conclusion that the US measures followed the recommendations of the DSB.

The two countries came to an agreement on September 21, 2006 to comprehensively resolve this dispute; it became effective on October 12, 2006. Under the agreement the US ended its anti-dumping duties and countervailing duties retroactively and returned to Canada $4 of the approximately $5 billion in accumulated duties collected since 2002 (the remaining $1 billion is to
be applied to funds for the US lumber industry), and agreed not start a new investigation during the effective period of the agreement. Meanwhile, when domestic prices in the US fall below a given standard, Canada should either collect an export tax, or combine an export tax with limitations on export quantities. Specifically, export taxes will be between 0% and 15%, depending on the monthly average of softwood lumber prices. When the market share of Canadian lumber in the US falls, Canada will return the export taxes it has collected to the exporters.

The US claimed that Canada violated the agreement on the grounds that Canada did not consider the decrease in consumption in the US when determining the export amount based on which additional import control measures would be issued. In August 2007, the US filed a complaint in the International Court of Arbitration in London. In January 2008, the US filed a second suit claiming that the tax cut and subsidies offered by the provinces of Quebec and Ontario were circumvention of export control measures that Canada had agreed not to take. However, In January 2011, the court acknowledged an SLA violation by Canada. In accordance with this arbitration, in March of the same year, Canada began to impose additional export tax on exports from Quebec and Ontario.

On July 18, 2012, the International Arbitration Court dismissed the appeal made by the United States that the cost of timber harvested in the public domain of British Columbia fell below the SLA standards. The United States was not satisfied with this decision, and it expressed the intention to monitor developments in Canada in the future.

In January 2012, both countries agreed to extend the SLA deals that expire in October 2013 for two years until 2015. Hence, hereafter based on the SLA, cases may be filed in the International Court of Arbitration.

6. **DISPUTES ON EU SUGAR SUBSIDIES (DS265, DS266, DS283)**

(Please see page 442 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

7. **DISPUTE ON US COTTON SUBSIDIES (DS267)**

(Please see pages 442-443 in the 2016 Report on Compliance by Major Trading Partners with Trade Agreements –WTO, FTA/EPA and IIAs-)

8. **TAX TREATMENT FOR EXPORT COMPANIES (ETI REGIME; FORMERLY FSC REGIME) (DS108)**

The United States excluded from taxable income a portion of the export revenues generated by foreign sales corporations (“FSC”, i.e., companies that sell or lease outside of the United States goods produced in the United States), provided these revenues include above a certain threshold of US products. Also, a parent company could treat dividends paid to it by an FSC as non-taxable income. The regime was employed mainly by US parent companies exporting their products through foreign subsidiaries.

In November 1997, the EU requested WTO consultations with the United States, claiming that the regime represented an export subsidy and a subsidy contingent upon the use of domestic goods over imported goods prohibited under Article 3 of the Agreement on Subsidies and Countervailing Measures (ASCM). Consultations were held between the United States and the EU, but they were unable to reach an agreement. In September 1998, a panel was established. Japan participated in the panel proceeding as a third party. The Panel Report was issued in October 1999 and found that
the tax exemptions granted under the FSC program constitute export subsidies in violation of the Agreement. The Report recommended that the United States eliminate the regime by October 2000. However, the Panel did not rule on whether the program was a subsidy contingent upon the use of domestic goods over imported goods. The United States appealed the panel ruling, while the EU requested Appellate Body review of whether the program was a subsidy contingent upon the use of domestic goods over imported goods. Japan again participated as a third party. In February 2000, the Appellate Body upheld the panel ruling. In light of the Appellate Body ruling, the US declared that it would repeal the FSC program by November 1, 2000. Congress repealed the FSC and replaced it with the Extraterritorial Income Exclusion Act of 2000 ("ETI") signed by the President on November 17, 2000. The US claimed that the ETI: (1) expands the scope of tax deductions by not requiring that products (including services) be produced within the United States, so that the ETI does not constitute an export subsidy; and (2) amends the Internal Revenue Code of 1986 to exclude tax deductions for the income derived from foreign sales or leasing of products (including services) produced under certain conditions, therefore not creating a subsidy as defined in the Agreement. The EU criticized the ETI for: (1) maintaining the condition that sales be outside the United States, so that the ETI still provides an export subsidy; (2) requiring at least 50 percent US content, so that the ETI also provides a subsidy contingent upon the use of domestic over imported goods; and (3) containing a transitional measure allowing the FSC program to continue to operate after November 2000 for the foreseeable future, thereby violating the DSB decision that the regime be eliminated by November 1, 2000. The EU thus argued that the ETI continues to violate the ASCM. A panel was established to judge the WTO consistency of the ETI pursuant to Article 21.5 of the DSU. The EU also submitted a list of US products that could be subject to sanctions, preparing to invoke countermeasure.

In August 2001, the panel upheld the claims of the EU and Japan and found that the ETI provides an export subsidy prohibited under the ASCM and the Agreement on Agriculture and that its local content requirement violates GATT Article III (national treatment). In October 2001, the US appealed to the Appellate Body, arguing that the ETI did not comprise an export subsidy in that the method used to receive tax breaks was not restricted to exports and that there was accordingly no direct causal link between the ETI and exports. In January 2002, the Appellate Body upheld the panel’s decision.

One of the major points of contention with regard to the ETI pertains to the relation between the ASCM and the prevention of double taxation of income for which tax is withheld abroad. The US claimed that, because the ETI was a system designed to prevent double taxation on such income, it was permitted under Footnote 59 of the ASCM Annex I, and, therefore, did not constitute an export subsidy banned under the Agreement. The EU and Japan rejected this argument on the grounds that the ETI was little more than a whitewashed version of the FSC regime and was clearly an export subsidy. Moreover, the EU and Japan argued that it was unlikely that the system was designed to prevent double taxation, as the US claimed, because the scope of the tax breaks under the ETI was selective. In August 2002, a WTO arbitrator concluded that the US$4 billion tariff concessions proposed by the EU constitutes appropriate countermeasures.

The US American Jobs Creation Act of 2004 (the Act), which repealed the ETI, was signed into law on October 22, 2004. The EU had imposed retaliatory measures on March 1, 2004, but agreed to temporarily suspend them when the Act took effect on January 1, 2005. However, to determine whether the Act complies with the rulings of the WTO, the EU requested the establishment of a WTO Article 21.5 compliance panel; the panel was established on February 17, 2005. The EU argued that the transition provisions of the ETI and the fact that the ETI will remain in effect for any contract signed before September 17, 2003 (grandfathering provision) are inconsistent with the WTO Agreements.
In response, the United States did not contest the first Article 21.5 panel’s findings. Instead, the United States argued that the first 21.5 panel made no new recommendation regarding the Act. The United States maintained its position that the recommendations of the first 21.5 Panel and the Appellate Body were not related to the ETI. The Panel rejected the US’s argument and concluded that the United States maintained prohibited FSC and ETI subsidies through the transition and grandfathering measures at issue, and that it continued to fail to implement fully the operative DSB recommendations and rulings to withdraw the prohibited subsidies. The Panel Report was circulated on September 30, 2005. The United States appealed to the Appellate Body, and the EU also appealed on November 27, 2005. The Appellate Body upheld the 21.5 Panel’s findings, concluding that the US still had not implement the recommendation. The Appellate Body report was circulated in February 2006.

In May 2006, the US Congress passed a bill that included provisions to repeal the grandfathering provisions in the US Job Creation Act of 2004. In consideration of this, the EU adopted a Council Resolution to extend the period to repeal sanctions through May 29, 2006 or, if President Bush signed the tax reduction bill by May 26, to repeal the regulations providing for sanctions measures effective May 29. President Bush signed the bill on May 17; therefore, the resolution invoking sanctions was repealed effective May 29.

COLUMN:
IMPORTANCE OF ENHANCEMENT OF DISCIPLINE FOR IMPROVED TRANSPARENCY OF SUBSIDIES

1. Awareness of Issues

All around the world, many companies whose businesses have already substantially failed (commonly known as “zombie companies”) manage to survive because of various subsidies, financial support, or implicit guarantee provided by the government directly or indirectly through state-owned companies, etc., which have caused such problems as market distortion and excess supply. At the 2017 G20 Hamburg Summit, the leaders declared that excess capacity was a global issue that requires coordinated response by all countries and called for the abolishment of subsidies provided by governments and their related agencies that may have been distorting the market and caused the state of excessive supply. One of the factors that makes it difficult to address the issue of unfair supports provided by governments and related agencies is the scarcity of information concerning such supports. In particular, various indirect aids provided through government-related agencies, including low-interest loans from state-owned banks, make it even more difficult to capture the situation. WTO Members are obliged to notify the Committee on Subsidies and Countervailing Measures (“Subsidies Committee”) of any subsidies for specific entities, whether they be directly or indirectly provided from governments. However, some have pointed out that this notification system has not been functioning effectively.

This Column gives an overview and explains the limit of aforementioned disciplines to secure the transparency of subsidies. Then, it outlines the ongoing efforts for enhancing these disciplines.

2. Existing Disciplines for Transparency

In order to enhance the transparency of government-granted subsidies, the WTO requires its
Members to notify subsidies that are specific in their nature (Article 25.2 of the ASCM). Article 25.3 of the ASCM provides that the content of notifications should be sufficiently specific to enable other Members to evaluate the trade effects and to understand the operation of notified subsidy programs. Specifically, items to notify include the following.

- Form of a subsidy (i.e. grant, loan, tax concession, etc.)
- Subsidy per unit or, in cases where this is not possible, the total amount or the annual amount budgeted for that subsidy (indicating, if possible, the average subsidy per unit in the previous year)
- Policy objective and/or purpose of a subsidy
- Duration of a subsidy and/or any other time limits attached to it
- Statistical data permitting an assessment of the trade effects of a subsidy

Notified information is publicized on the WTO website and made publicly accessible.³ Japan also notified 52 subsidy programs in the latest report of 2017. However, since non-compliance with the obligation to notify is not subject to any penalty, not all countries have complied with the obligation, which is the reason why the notification system has not been functioning sufficiently. For example, according to the WTO report issued in March 2017 (G/SCM/W/546/Rev.8), only 62 countries out of all 162 Members (38%) made subsidy notifications in 2015.

As a means to complement the above notification system, WTO Members are allowed to make inquiries about other Members’ subsidies that have not been notified (Article 25.8 of the ASCM). WTO Members are also allowed to bring subsidies to the notice of the Subsidies Commission on behalf of another Member (“cross-notification”) (Article 25.10 of the ASCM). However, as there is no deadline for responding to inquiries about yet-to-be-notified subsidies (Article 25.9 of the ASCM), countries that have received inquiries have not always answered their questions promptly. In fact, the United States registered agendas to demand China to comply with the notification obligation at every meeting of the Subsidies Committee. The EU also pointed out the importance of the notification obligation during the discussion concerning excess supply and subsidies at the sessions of the Subsidies Committee. Moreover, the cross-notification system has not been effectively functioning as a means to enhance the transparency of subsidies, because it requires a Member making a cross-notification to be aware of the details of the subsidy it is bringing to the Subsidies Committee.

3. Efforts to Enhance the Disciplines for Transparency

With the understanding that the lack of incentives for Members to notify subsidy programs is one of the reasons why the notification system has failed to work effectively, as mentioned above, Japan, the EU, and the United States submitted the following proposals to enhance incentives to make subsidy notifications.

The EU submitted an ambitious proposal to drastically change the conventional legal rights and

³ [https://www.wto.org/english/tratop_e/scm_e/scm_e.htm](https://www.wto.org/english/tratop_e/scm_e/scm_e.htm)
obligations under the ASCM, which may even require the amendment of the ASCM, such as presuming yet-to-be-notified subsidies as subsidies causing “serious prejudice” to the interest of other Members as provided under Article 6 of the ASCM. The proposal from the United States was also an ambitious one, which suggested imposing disadvantageous measures on Members not complying with the notification obligation. These two proposals seem unlikely to be endorsed by other Members immediately.

<table>
<thead>
<tr>
<th>Outline of the Proposal from EU</th>
</tr>
</thead>
<tbody>
<tr>
<td>In May 2017, the EU made the following proposals in the proposal document for the rule negotiation areas (TN/RL/GEN/188).</td>
</tr>
<tr>
<td>[i] Enhancement of incentives to notify</td>
</tr>
<tr>
<td>Proposed the introduction of a provision to presume subsidies which have not been notified or subsidies which have been brought to the attention of the Subsidies Committee by a third Member based on Article 25.10 of the ASCM as subsidies causing “serious prejudice” to the interest of other Members (actionable subsidies).</td>
</tr>
<tr>
<td>[ii] Enhancement of monitoring</td>
</tr>
<tr>
<td>Proposed a system in which a Member levying a countervailing measure can check, when making a semi-annual report, whether the country subject to said measure has notified the Subsidies Committee of the subject subsidy and, if it finds such subsidy has not been notified, it can notify such subsidy to the Subsidies Committee.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Outline of the Proposal from Japan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan proposed the development of guidelines that must be complied with when Members receive requests for information based on Article 25.8, in order to clarify procedures for responding to inquiries regarding subsidies that have not been notified, which are made in accordance with Article 25.9 of the ASCM.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Outline of the Proposal from the United States</th>
</tr>
</thead>
<tbody>
<tr>
<td>In October 2017, the United States made the following proposals in the proposal document for the session of the WTO Council for Trade in Goods toward MC11 (JOB/GC/148, JOB/CTG/10).</td>
</tr>
<tr>
<td>1. Expand the scope of the agreements in which the obligation to notify the WTO is included (Agriculture Agreement, AD Agreement, Subsidies Agreement, SG Agreement, TRIMs Agreement, SPS Agreement, TBT Agreement, etc.)</td>
</tr>
<tr>
<td>2. Encourage Members to cross-notify subsidies on behalf of non-complying Members</td>
</tr>
<tr>
<td>3. Impose the following disadvantageous measures on non-complying Members</td>
</tr>
<tr>
<td>(When one year has elapsed from the notification deadline)</td>
</tr>
<tr>
<td>• Suspension of qualification to become a Chairman of a committee;</td>
</tr>
<tr>
<td>• Circulation of documents;</td>
</tr>
<tr>
<td>• Suspension of access to the WTO Members website;</td>
</tr>
<tr>
<td>• Annual contact from Director General to the Minister in charge of WTO affairs; and</td>
</tr>
<tr>
<td>• Obligation to give an explanation at a General Council meeting.</td>
</tr>
</tbody>
</table>
Part II: WTO Rules and Major Cases

4. Future Issues

The enhancement of discipline to secure subsidies’ transparency is essential in addressing the issue of market-distorting supports by governments and their related agencies. It is necessary to continue the discussion concerning this matter through various forms, develop an effective disciplinary mechanism, and expand the circle of endorsement for it. Japan supports the objectives of the proposals made by the United States and the EU and the direction these proposals intend to lead WTO Members to, as they would be beneficial in enhancing the enforcement of the current WTO rules. As a more feasible measure that would be more easily accepted by other Members, Japan has proposed to develop guidelines to facilitate the effective use of the inquiry system, such as defining a deadline to respond to inquiries made pursuant to Article 25.9 of the ASCM. Japan hopes to have thorough discussion with other Members on this matter, while also conducting detailed analysis of the proposals.

In addition, the issue of how we could enhance procedures to secure transparency and the issue of what kind of subsidies needs to be regulated are interrelated with each other. The scope of entities and the forms of subsidies to be regulated need to be discussed.

Even when notification to the WTO Subsidies Committee has not been made, information regarding the subsidy in question may already be publicized according to the requirement of the applicable domestic law. It is important to include various ways to tackle this issue in consideration (such as promoting the disclosure of subsidy-related information via policy reviews), while keeping in mind that notification to the WTO Subsidies Committee is one of the ways to enhance the transparency of subsidies.