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SPECIFICITY

Communication from Canada

The following communication, dated 21 May 2004, is being circulated at the request of the Delegation of Canada.

The submitting delegation has requested that this paper, which was submitted to the Rules Negotiating Group as an informal document (JOB(04)/54), also be circulated as a formal document.

I. ISSUE

1. The concept of "specificity" is one of the cornerstones of the WTO *Agreement on Subsidies and Countervailing Measures Agreement* (ASCM). It has been generally recognized for nearly 20 years now that this important concept would benefit from precision in its application.[1] A review of the many interpretations of this requirement and the significant domestic litigation it has caused over this period of time reinforces the need to establish certain checks to the discretion afforded to investigating authorities in its application.[2] Given the fact that all remedies under the ASCM require a specificity finding, the concept would benefit from further clarification.

2. The amendments proposed in this document attempt to strike a balance between the need to establish clear and objective standards for the application of Article 2 of the ASCM, and the need to retain the necessary flexibility to address different facts in different cases. It is believed that such amendments would result in a clearer and more predictable specificity test. In this regard, the discussion below does not purport to be an exhaustive enumeration of relevant issues. This document is simply intended to promote a technical discussion on the specificity requirement. Canada reserves the right to offer additional thoughts on the matter.

II. GENERAL PRINCIPLES

3. The purpose of the specificity requirement in Article 1.2 of the ASCM is to ensure that the disciplines in the Agreement cover only those subsidies that are targeted to certain entities or productive activities, i.e. subsidies that go to some entities over others. The panel in *US – Export Restraints* explained:

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[1] "Draft Guidelines for the Application of the Concept of Specificity in the Calculation of the Amount of a Subsidy Other Than an Export Subsidy", SCM/W/89 (25 April 1985)

[2] See for example: J.H. Bello, & A.F. Holmer, "US Trade Law and Policy Series #12: The Specificity Dialogue Continues", (1988) 22:2 International Lawyer, 563; J.C. Lowe & D. Mason, Jr., "Recent Highlights in Commerce's Application of the 'Specificity Test' Under Countervailing Duty Law" (1994) 864 PLI/Corp 39; J.A. Ragosta & H.M. Shanker, "Specificity of Subsidy Benefits in US Department of Commerce Countervailing Duty Determinations", (1994) 25 Law & Pol'y Int'l Bus 639.

> "[W]hile the object and purpose of the Agreement clearly is to discipline subsidies that distort trade, this object and purpose can only be in respect of 'subsidies' *as defined* in the Agreement. This definition, which incorporates the notions of 'financial contribution', 'benefit', and 'specificity', was drafted with the express purpose of ensuring that not every government intervention in the market would fall within the coverage of the Agreement" (emphasis in original);[3]

III. CERTAIN CONCEPTS REQUIRING CLARIFICATION

A. "ENTERPRISE", "INDUSTRY", AND "GROUP"

4. The phrase "enterprise or industry or group of enterprises or industries", in respect of which specificity must be established, encompasses a sizeable universe of analysis. Yet, there is no clear guidance in the ASCM on the meaning of "enterprise" and "industry", nor on how the respective groupings are circumscribed. This lack of clarity results in uncertainties in the application of the specificity test.

5. Most recently, the panel in *US – Softwood Lumber IV* was required to determine whether Canada's forestry management programmes were specific to a group of industries. It noted:

> "The SCM Agreement does not define an 'industry' nor does it provide for any other rules concerning which enterprises could be considered to form an industry for the purposes of Article 2 of the SCM Agreement or whether a group of industries has to produce certain similar products in order to be considered a 'group'."[4]

6. The panel went on to identify certain "industries" in its own terms, and to determine that they constituted a "limited group" without reference to any objective standard.[5] Better guidance on the identification and assessment of industries for specificity purposes would assist both investigating authorities and WTO dispute settlement panels, and would provide Members with a clearer and more predictable rule.

B. DE FACTO SPECIFICITY

7. Two aspects of the *de facto* specificity test would also benefit from clarification.

8. First, the weight of the four *de facto* specificity factors in Article 2.1(c) of the ASCM should be made more explicit. That is, where a subsidy is *de jure* generally available and the exercise of government discretion has been neutral and objective, any use by a limited number of certain enterprises, predominant use or disproportionate grants during a particular period of time may be due

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[3] *United States – Measures Treating Export Restraints as Subsidies*, Report of the Panel, WT/DS194/R and Corr.2, adopted 23 August 2001, para. 8.63. See also *Indonesia – Certain Measures Affecting the Automobile Industry*, Report of the Panel, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, adopted 23 July 1998, para. 14.155, and *United States – Final Countervailing Duty Determination with respect to Certain Softwood Lumber from Canada*, Report of the Panel, WT/DS257/R, adopted 17 February 2004, para. 7.116 ("Article 2 SCM Agreement is concerned with the distortion that is created by a subsidy which either in law or in fact is not broadly available.").

[4] *US – Softwood Lumber IV, supra* note 3, para. 7.119

[5] *Ibid.*, para. 7.121:

> "We consider that the 'wood products industries' constitutes at most only a limited group of industries – the pulp industry, the paper industry, the lumber industry and the lumber remanufacturing industry – under any definition of the term 'limited'."

solely to situational circumstances. For example, any "predominant use by certain enterprises" during a given time period may be solely the result of certain enterprises being first off the mark.

9. Second, there is currently no clear guidance in the ASCM on the particular application of any of the four factors set out in Article 2.1(c). A case in point is the application of the "disproportionately large grants" factor. An application of this factor based on a strict comparison of absolute subsidy amounts going to eligible recipients ignores the reality that disbursements to a particular enterprise or industry may be larger or smaller, depending on the relative importance of the enterprise or industry in a given sector of the economy. For example, a finding that there existed "the granting of disproportionately large amounts of subsidy to certain enterprises" would be justified if a given group of agricultural industries, which accounted for 30 per cent of the value of total agricultural production, was found to have received 70 per cent of available subsidy amounts. However, such finding would not be justified if the group of industries in question received 30 per cent of available subsidy amounts.

IV. PROPOSED AMENDMENTS

A. "ENTERPRISE", "INDUSTRY", AND "GROUP"

Amendment 1

10. It is proposed that the phrase "*in accordance with international standard industrial classification and*" be added to Article 2.4 of the ASCM. The amended provision would thus read:

> "Any determination of specificity under the provisions of this Article shall be <u>in accordance with international standard industrial classification and</u> clearly substantiated on the basis of positive evidence."

11. The added text would serve to reference current objective classifications, namely the United Nations *International Standard Industrial Classification of All Economic Activities* (ISIC).[6] The ISIC, as revised from time to time, is well-suited for specificity analysis: it already objectively identifies and names industries, and groups them into various levels of aggregation; it has been in existence for nearly as long as the GATT; it enjoys wide recognition internationally; and it is already used by the WTO in the production of world trade statistics. Indeed, the ISIC represents the most current international understanding of the concepts of "industry" and "enterprise".[7]

12. The rationale behind this amendment is that it would require domestic investigating authorities to request and assess evidence on the availability or use of a subsidy in terms of established industry codes and aggregations. Accordingly, it would require such authorities, as well as WTO dispute settlement panels, to make factual findings that would be more clearly based on widely accepted international standards.

B. DE FACTO SPECIFICITY

Amendment 2

13. It is proposed that the Agreement expressly confirm that the mere existence of any of the four factors does not automatically establish specificity, i.e. that a specificity finding that ignores the totality of the facts of a given case would not be sustainable. Accordingly, the following phrase should be added between the second and third sentences of Article 2.1(c): "These factors shall be

[6] Currently ISIC Rev.3.1, ESA/STAT/SER.M/4/Rev.3.1.
[7] ESA/STAT/SER.M/4/Rev.3.1, para. 15 ("industry"), and paras. 53-57 ("enterprise").

evaluated based on the totality of the facts, and no one or several of them can necessarily give decisive guidance." The amended provision would thus read:

> "(c) If, notwithstanding any appearance of non-specificity resulting from the application of the principles laid down in subparagraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of a subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy. <u>These factors shall be evaluated based on the totality of the facts, and no one or several of them can necessarily give decisive g</u>uidance. In applying this subparagraph, account shall be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority, as well as of the length of time during which the subsidy programme has been in operation."

14. This amendment would confirm that *de facto* analysis involves an assessment of the totality of the facts of a given case. It would recognize that situational circumstances beyond the control of granting authorities might explain use or distribution patterns of a subsidy that is otherwise *de jure* non-specific under subparagraphs (a) and (b). Such an amendment would therefore expressly preclude any arbitrary automaticity in the application of the factors in subparagraph (c), e.g., where an investigating authority determines *de facto* specificity based solely on the existence of one of the listed factors, notwithstanding any reasonable explanation for the existence of that factor or any other evidence of non-specificity.

Amendment 3

15. It is proposed that a footnote be added to the end of the phrase "the granting of disproportionately large amounts of subsidy to certain enterprises" in Article 2.1(c) requiring that disproportionality be determined with reference to a relevant objective benchmark, such as the relative importance of recipient industries, in terms of production value, within the jurisdiction of the granting authority.

16. This amendment would clarify that while the distribution of subsidy amounts may appear disproportionate when viewed on an absolute basis (i.e. a strict comparison of subsidy amounts among recipient industries for a given period), such distribution may in fact be proportionate because amounts received by the industries in question were in proportion to their share of the production value of the relevant economic sector.