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REQUEST FOR CONCILIATION UNDER
ARTICLE 17 OF THE AGREEMENT

Communication from the United States

The United States Trade Representative has requested that the attached information be brought to the attention of Signatories.

THE UNITED STATES COMPLAINT AGAINST THE EUROPEAN
COMMUNITY CONCERNING WHEAT FLOUR EXPORT SUBSIDIES

This information and background material has been provided by the United States Delegation with a view towards enabling the Committee to review the facts of the case as provided for under Article XVII:1 and towards facilitating the conciliation process. The statement discusses the nature of the EC subsidy, the history of U.S. - EC consultations on this dispute, and the reasons why the United States believes that EC export subsidies on wheat flour have been granted in a manner inconsistent with Articles 8 and 10 of the Subsidies Code and Article XVI of the GATT.

EC export subsidies for wheat flour: The existence of EC export subsidies for wheat flour is beyond dispute. Community-wide export subsidies for wheat flour have been granted since 1967 with funds provided through the European Guarantee and Guidance Fund (better known by the French acronym FEOGA). However, during a brief period in 1973-75, when world wheat prices rose above EC support levels, EC export subsidies for wheat flour were eliminated and, in fact, taxes were imposed on flour exports. During the period 1962 to July 1967, when national grain prices were being steadily aligned, the individual member states were authorized to grant export subsidies on wheat flour. Export subsidies for wheat flour normally benefit from advance fixing - i.e., the subsidy applicable on the day on which the export license application is submitted

may be fixed for a certain time period, normally 4 months plus the month of issue. Where this is not done, the subsidy applicable on the day of exportation is granted.

The basic statutory authority for the granting of EC export subsidies on wheat flour is Regulation No. 2727/75 (formerly 120/67), which established an EC-wide system governing the marketing of grains and grains products. The so-called grains CAP established common target and intervention prices for wheat and other grains in the Community. In all but a few exceptional years, these prices have been well above world market price levels. To protect EC grain prices against competition from lower-priced imports, the variable levy system was established. To enable the Community to sell grains and grain-based products in world markets, export subsidies were provided for. The preamble to Regulation No. 2727/75 states that: "Provision should be made for charging a levy on imports from third countries and for the payment of a refund on exports to these countries, both being designed to cover the difference between prices ruling outside and within the Community; whereas, moreover, in respect of products processed from cereals to which this Regulation applies, account should be taken of the need to ensure a measure of protection for the Community processing industry."

Guidelines for the determination of wheat flour export subsidies are provided in EC Regulation No. 2746/75. This Regulation identifies the "specific criteria" to be taken into account in fixing the subsidy as: a) grain prices on the various Community markets; b) the quantity of grain needed to produce one unit of flour and the value of milling

by-products; and c) possibilities and conditions for the sale of flour on the world market. These guidelines obviously leave the Commission great flexibility in establishing subsidies. An examination of the methods actually used by the Commission in calculating subsidies (too complex to be discussed in this paper) makes even clearer the arbitrary nature in which the subsidy is fixed.

Over the past two EC marketing years, Community export subsidies have been as high as 92.50 ECU/MT -- representing nearly 50 percent of the representative U.S. FOB price for flour (GULF).

U.S. - EC consultations: Notable in this dispute is the number of times the United States has attempted to resolve it through consultations with the European Community. Formal consultations under GATT Article XXII:1 were first held on February 14, 1977; Australia and Canada joined in these consultations. In subsequent years, there followed numerous informal discussions with the Community, another round of GATT Article XXII:1 consultations in October 1980, and two "technical consultations" earlier this year. None of these meetings moved the issue closer to resolution.

It is worth pointing out that during this period of consultation, the EC's commanding share of the world market continued to expand. In the 3 years prior to the initiation of consultations in February 1977, EC commercial exports already totaled about 65 percent of total world commercial exports; in the latest 3-year period for which data are available (1977/78 - 1979/80), this share has risen further to over 70 percent. Similarly, the volume of EC commercial exports rose from an average of about 2.4 million MT to more than 3 million MT over this period.

Given the lack of progress in earlier bilateral consultations, on September 29, 1981, the U.S. requested consultations with the Community on their wheat flour export subsidies under Article 12 of the Agreement on Interpretation and Application of Articles VI, XVI, and XIII of the GATT (Subsidies Code.) These consultations were held on October 28, 1981. As the Community again showed no inclination to move towards a "mutually acceptable solution" of the dispute, the United States has referred the matter to the Committee for conciliation as provided for in Article 13 of the Code.

U.S. case under the Subsidies Code: It is clear that EC export subsidies on wheat flour are granted in a manner inconsistent with Articles 8 and 10 of the Code, as well as Article XVI of the GATT. The U.S. further considers that such subsidies cause nullification or impairment of benefits accruing to the United States under the GATT and serious prejudice to U.S. interests. More specifically, we believe that:

A. EC subsidies on the export of wheat flour are applied in a manner which results in the EC having more than an equitable share of the world export trade in violation of Article 10 (1) of the Code and Article XVI:3 of the GATT.

Article 10 (1) of the Code coincides with Article XVI:3 and states:

"Signatoires agree not to grant directly or indirectly any export subsidy on certain primary products in a manner which results in the signatory granting such subsidy having more than an equitable share of the world export trade in such product, account being taken of the share of the

signatories in trade in the product concerned during a previous representative period, and any special factors which may have affected or may be affecting trade in such product."

Further guidance as to the interpretation of the phrase "more than an equitable share" is provided by Article 10:2 (4) of the Code which states that it shall "include any case in which the effect of an export subsidy is to displace the exports of another signatory bearing in mind the developments of world markets."

As the figures in Table 1 clearly demonstrate, there has been a dramatic shift in market shares over the past two decades to the advantage of the EC and to the disadvantage of all other suppliers. The EC share of total commercial wheat flour exports has risen from an average of 28 percent in the early 1960's to over 70 percent in the most recent 3-year period. The shares supplied by the U.S., and by other significant exporters such as Australia and Canada, have shown very sharp and dramatic declines over this same period. This shift has been particularly damaging to non-EC suppliers because of the decline in total world export volume over this same period. As was noted earlier, EC aggrandizement has not ceased in recent years - in spite of the fact that EC exporters had already obtained an overwhelmingly dominant position on the world market by the early 1970's.

Given the long history of aggressive EC subsidization of wheat flour exports, the U.S. believes that examination of the evolution of the wheat flour market over the past two decades is appropriate in determining whether the EC has gained an inequitable share of the world flour market. It

is only over this period that the unfolding of the EC export subsidy policy for wheat flour can be fully comprehended. There is GATT precedent for this: In determining that French export subsidies for wheat and wheat flour were applied in a manner inconsistent with the GATT, a 1958 GATT panel examined a similarly long period (L/924). Article 10(2)(C) of the Code provides: "A previous representative period shall normally be the three most recent calendar years in which normal market conditions existed". Clearly, this provision is meant to be flexible, to serve only as a guide. In our view, it is equally clear that "normal market conditions" have not existed for some time in the world wheat flour market due to the determined use of subsidies by the EC to gain and maintain dominance in that market.

While the concept of "more than an equitable share" has not been defined precisely, it is clear that the massive share of the market gained by the EC -- attributed only to its heavy use of export subsidies -- is inequitable by any reasonable interpretation.

In view of the dramatic shift in market shares shown in Table 1, there is no doubt that the EC's subsidized wheat flour exports have displaced the U.S. and other suppliers in violation of Article 10 (2). The expansion of EC exports - in an overall declining market - could only have come at the expense of the other exporters. In the case of the United States, this situation has resulted in our virtual exclusion from markets in which we were formerly active commercially and from new markets developed in more recent years. In several key markets, there has been a sizeable reduction in the U.S. share.

B. EC subsidies on the export of wheat flour are applied in a manner which results in prices materially below those of other suppliers to the same market in violation of Article 10 (3) of the Code.

During the course of bilateral consultations on this issue, the United States has brought numerous examples of price undercutting to the EC's attention. Table 2, which summarized the results of tenders on flour sales to certain specific markets, show several of the more recent examples of this practice. In the October 1980 Yemen tender, the EC underbid the United States by nearly \$70/MT; in the February 1980 Sri Lanka tender, by nearly \$40/MT; and in the May 1981 Yemen tender, by more than \$100/MT. Obviously, it is difficult to obtain price data for specific markets, not all of which import via public tenders; the United States believes, however, that the complete dominance of world flour markets achieved by the Community through the use of export subsidies is itself evidence of price undercutting. The EC could not have obtained such a dominant position were it not for its policy of granting whatever amount of subsidy is required to underprice its competitors and thus gain a particular market. Moreover, our examination of EC export subsidies for wheat flour over the past few years shows that they are habitually larger than can be justified in terms of the differential between EC and world wheat prices. Thus, generating a built-in bias towards price undercutting on the world flour market.

C. EC subsidies on the export of wheat flour are causing nullification or impairment of benefits accruing to the U.S. under the GATT and serious prejudice to the interests of the United States in violation of Article 8:3 of the Code.

Article 8:3 (C) of the Code provides that signatories should avoid causing, through the use of any subsidy, serious prejudice to the interests of another signatory. Article 8:4 (C)

further provides that serious prejudice may arise specifically through "the effects of the subsidized exports in displacing the exports of like products of another signatory from a third country market." The EC's achievement of an inequitable share of the world market, the resultant displacement of U.S. exports, and the chronic price undercutting practices by the Community, have all caused serious prejudice to U.S. interests. Moreover, the U.S. believes that the arbitrary manner in which EC export subsidies for flour are set and the lack of any pre-established limits on EC production, prices or subsidies, both of which render other exporters unable to compete, cause serious prejudice to U.S. interests. The manner of subsidization creates a permanent source of uncertainty in the world wheat flour market.

Nullification or impairment of benefits accruing under the GATT results from violation of assurances implicit in the GATT and the Code that EC export policies would be conducted in a manner consistent with its obligations under GATT Article XVI and Articles 8 and 10 of the Code. Footnote 26 to Article 8:4 of the Code states that:

"Signatories recognize that nullification or impairment of benefits may also arise from the failure of a signatory to carry out its obligations under the General Agreement or this Agreement. Where such failure concerning export subsidies is determined by the Committee to exist, adverse effects may ... be presumed to exist..."

The United States believes that the EC has clearly violated these obligations, that it has consequently nullified or impaired benefits to the U.S. and other major exporters, and that adverse effects may be presumed to exist.

TABLE 1
RELATIVE SHARES OF THE WORLD COMMERCIAL FLOUR MARKET

(1,000 Metric Tons Wheat Equivalent)

	Average 1959/60-61/62		Average Most Recent 3-Year Period 1977/78-79/80	
	Volume	Share (%)	Volume	Share (%)
European Community	1,392	28	3,125 ^{1/}	71
United States	1,354	28	471	11
Australia	820	17	88	2
Canada	1,017	21	568	13
Other	286	6	117	3
TOTAL	4,869		4,370	

^{1/} EC food aid shipments have not been broken out separately in data submitted to the International Wheat Council over this 3-year period. Based on EC wheat flour aid levels in the previous 6 years, we have estimated such shipments at 10.8 percent of total exports and deducted these amounts in estimating EC commercial shipments for 1977/78-1979/80.

TABLE 2
 WHEAT FLOUR: EXAMPLES OF PERFORMANCE
 UNDER SPECIFIC TENDERS (PRICES IN \$/MT)

<u>Date, Country and Basis</u>	<u>Average EC Bid</u>	<u>EC ^{1/}</u> <u>EC Bid Accepted</u> <u>\$/MT</u>	<u>EC Subsidy</u>
A. Feb. 1980, Sri Lanka, C&F	318.34	308.91 ^{2/}	105.00
B. Oct. 1980 Yemen, C&F	331.00	309.00	91.00
C. May 1981 Yemen, C&F	312.89	291.70	67.80

	<u>Bid</u>	<u>U.S.</u> <u>Difference Between EC Bid</u> <u>Accepted and U.S. Bid</u>
A.	348.50	39.59
B.	378.00	69.00
C.	403.87	112.17

TABLE 2

<u>OTHER EXPORTERS</u>		
<u>Country</u>	<u>Average Bid</u>	<u>Lowest Bid</u>
A. Canada	300.90 ^{3/}	300.90 ^{3/}
Argentina	330.50	330.50
B. Australia	384.50	383.00
Canada	398.00	398.00
C. N/A	N/A	N/A

1/ On the February 1980 tender, there were 11 EC bids; on the October 1980 tender, 8; on the may 1981 tender, 11 EC bids and 3 bids of unspecified European origin.

2/ Other EC bids accepted at \$312.35 and \$314.41

3/ Offered FAS or FOB