CHAPTER 12

SUBSIDIES

The *Charter* does not forbid the use of subsidies for such purposes as the promotion of economic development, the diversification of industry, or the protection of national security. This method is to be preferred, in general, to the employment of devices that operate to restrict imports. Its cost is clear and taxation can distribute its burden equitably among those who benefit.

Any subsidy that affects the ability of domestic producers to compete with foreign producers, either at home or abroad, will exert an influence on the flow of trade. This will be true whether the subsidy is direct or indirect, whether it is open or concealed, and whether it operates to reduce imports or to increase exports from the levels that would otherwise obtain. The direct subsidization of exports, however, is particularly likely to interfere with the maintenance of good relations in international trade.

When a country subsidizes exports, it gives its own producers an advantage over producers located in the countries where its goods are sold and over those located elsewhere who also compete in these markets. Its action is certain to be regarded as an unfair method of competition and retaliation is likely to result. The countries in which it sells may seek to exclude its goods by imposing countervailing duties, by raising tariffs, or by establishing import quotas. The countries with which it competes may attempt to maintain their position by matching its subsidies or to better it by paying even higher ones. In either case, the subsidization of exports will arouse resentment and invite antagonistic policies.

Most nations resort to artificial measures of one kind or another in the interest of domestic producers of agricultural commodities. The United States is no exception to the rule. If it chose to do so, it could increase the incomes of farmers by paying subsidies that would not affect the prices at which they sell. But it has chosen, instead, to support these prices at levels above those prevailing in the markets of the world. Such measures, of course, are inconsistent with the philosophy of free markets and private enterprise. They require that the domestic structure of prices and production be insulated against changes that occur abroad and obstruct their adaptation to the shifting conditions of supply and demand. But they represent an established policy of the United States. And, under this policy, commodities that bring higher prices at home cannot be sold abroad unless their exportation is subsidized. For this reason, the provisions of the *Charter* that deal with subsidies are of particular interest to the United States.

SUBSIDIES IN GENERAL

A member of the ITO who grants any subsidy that operates, directly or indirectly, to reduce imports or to increase exports must inform the Organization concerning the character of the subsidy, its extent, the reasons for its adoption, and its probable effects. If a subsidy threatens to injure the trade of another member, the country granting it may be called into consultation and must be prepared to consider the possibility that it might be modified. But beyond this its obligation does not go (25).

As a general rule, members undertake not to subsidize exports after the *Charter* has been in force for two years, a period which may be extended, upon request, by the ITO. Exemption of exports from taxes imposed on the domestic consumption of a commodity is not regarded as a subsidy. There are three exceptions to the general rule. Where a non-member grants a subsidy, a member may grant one to offset it (26). Where a member has a system of stabilizing domestic prices under which, as in Australia, those prices not only rise above but sometimes fall below the level at which it sells abroad, and if it does not so operate this system as unduly to stimulate exports or to injure other members, it may continue to pay the incidental subsidy. And finally, the wording adopted at Havana is so broad that it will probably permit any country to subsidize the exportation of primary commodities (27).

SUBSIDIES FOR AGRICULTURAL EXPORTS

The occasion for subsidizing exports usually arises, not when demand is large, supply small, and prices high, but when demand is small, supply extremely large, and prices seriously depressed. In these circumstances, it was suggested by the American *Proposals,* members of the ITO, instead of competing in subsidization, should seek relief through the negotiation of intergovernmental commodity agreements. If, in a particular case, an agreement could not be reached, or if an agreement should fail to accomplish the purposes for which it was designed, then the rule against subsidizing exports should be suspended until members decided that it should be reapplied.

This suggestion was incorporated in the London draft of the *Charter.* But at Geneva it was substantially modified. If negotiations directed toward the conclusion of a commodity agreement should break down, or if such an agreement should end in failure, under the provisions of the Geneva draft, a member might seek permission to subsidize exports from the ITO. This permission would be granted for a limited period and subject to specified conditions, if the ITO should determine that the commodity to be subsidized was in burdensome surplus, that the subsidy would not operate unduly to stimulate exports, and that the interests of other members would not be seriously prejudiced; otherwise, it would be refused. The United States objected to this change on the ground that the requirement of prior approval for the direct subsidization of agricultural exports was discriminatory. In the case of subsidies operating indirectly to reduce imports or increase exports, as do those of many other countries, no such approval was required. The position of the American delegation on this issue was therefore reserved.

At the Havana conference, the tighter provisions of the Geneva draft were accordingly relaxed. Under the present terms of the *Charter,* members who are paying export subsidies must cooperate in the negotiation of commodity agreements. And while such negotiations are in progress, they cannot initiate or increase such subsidies. But if negotiations do not succeed or promise to succeed, or if a commodity agreement is not thought to be appropriate, "any Member which considers that its interests are seriously prejudiced" by the rule against export subsidies will then be free to subsidize (27). The requirement of prior approval is thus abandoned. And the *Havana Charter* goes beyond the original American *Proposals* by permitting the inauguration of new subsidies, under these conditions, as well as the continuation of existing ones.

A FAIR SHARE OF THE MARKET

Export subsidies are a source of international irritation at any time. But they are particularly so when they are employed for the purpose of capturing an increasing share of the world's trade. It was accordingly suggested, in the American *Proposals,* that subsidization for this purpose should be banned. This suggestion was consistent with American practice: the United States has used subsidies to maintain its two-price system; it has not used them for the purpose of increasing its sales abroad. The principle that the exports subsidized by any country should not exceed its fair share of the world market was adopted by the Preparatory Committee and further developed at the Havana conference. And at Havana it was applied to all types of subsidies affecting trade.

A fair share of the market, according to the *Proposals,* would be the share prevailing in a previous representative period. To this the Preparatory Committee added the requirement that account be taken of special factors influencing the volume of trade. In the *Havana Charter,* these special factors are spelled out in more detail. Under its terms, consideration is to be given, not only to the situation existing in a previous representative period, but also to the importance of foreign trade in the commodity concerned to the country granting the subsidy and to countries materially affected by it, and to the desirability of expanding production in areas that are able to satisfy world requirements most economically and effectively.

In the London and Geneva drafts of the *Charter,* the representative period was to be selected initially by the country paying the subsidy, subject to consultation with other members at their request. Under the *Havana Charter,* an equitable share of the market is to be determined in the same way. But if consultation fails, within a reasonable period of time, to result in an agreement, a final determination can be made by the ITO (28). The Havana conference thus broadened the escape for subsidies on agricultural exports, applied a common principle to all types of subsidies affecting exports, and, in case of disagreement as to the application of that principle, provided for appeal and final settlement.

Unless there should be a radical change in American policy, it is unlikely that our own determination as to the quantity of exports to be subsidized would ever be called into question by other countries or, if it were, that differences could not be settled without appealing to the ITO. Here, as elsewhere, the *Charter* accommodates itself to American agricultural policy. On this score, at least, it will be rejected by economic purists and accepted by political realists.