Organisation for Economic Co-operation and Development

TAD/TC/GF/M(2019)1

For Official Use

English - Or. English

18 November 2019

TRADE AND AGRICULTURE DIRECTORATE
Trade Committee

Global Forum on Trade

OECD Global Forum on Trade

Levelling the Playing Field: Measuring and addressing trade-distorting Government Support

This summary record has been prepared by the OECD Secretariat. It represents the Secretariat's understanding of the discussion. It is not a formal record and does not bind participants in any way. The objective of this event was to provide an overview of the OECD's evidence-based approach to measuring government support and an opportunity to discuss, in a non-negotiating format, the growing concerns about practices which may be distorting trade and resulting in a less-than-level playing field. The event was held under Chatham House rules to facilitate a free-flowing exchange. Participants included senior level policy-makers from OECD and partner countries, and private sector representatives.

Contact: Gregor SLOKAN, Counsellor, Email: Gregor.slokan@oecd.org, Tel: +(33-1) 45 24 76 84.

JT03454863

This document, as well as any data and map included herein, are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

OECD Global Forum on Trade

Levelling the Playing Field: Measuring and addressing trade-distorting Government Support

23-24 October 2019, Paris, OECD

Summary record

Chatham House Rules

1. Main outcomes of the discussion

- In a context of global trade tensions there is an urgent need to begin updating the international trade rule-book to better address concerns about unfair competition in the global economy.
- Updating these rules benefits from robust information on the nature, scale and likely impact of current measures that can distort markets and detract from a level international playing field.
- The OECD has longstanding work measuring government support in agriculture, fossil fuels, and fisheries. It has recently estimated support and related market distortions in the aluminium value chain, and is also looking into a high technology sector (semiconductors).

1.1. Session: Agriculture

- There is potential for further international co-operation to promote agricultural reforms towards less trade-distorting government support, although progress is difficult and it can be challenging to identify low-hanging fruits in this area.
- OECD's work on measuring agricultural support is an important contribution to enhanced transparency, and the OECD is an important forum for the exchange of good practices in agriculture. The OECD should continue analysing domestic support to better understand the nature, scale and consequences of agricultural support, and to identify alternative policies that can achieve key goals without distorting international markets.

1.2. Aluminium

- The OECD report "Measuring distortions in international markets: the aluminium value chain" is impressively comprehensive and valuable as it injects much needed transparency into government support in the aluminium value chain.

- The work underscores the important role that government support has played in the increase in capacity seen in the aluminium sector. It underscores the need to take a value chain approach, as subsidies upstream confer significant support to downstream activities. Moreover, state entities emerge as important providers – and not just recipients – of government support, notably through the financial system, in the form of below-market loans. The influence of the state also has implications for the transparency of support policies.
- Clear and updated rules to address new distortions in industrial sectors such as the aluminium value chain remain to be developed. The establishment of new rules will need to go hand-in-hand with continuous efforts to ensure the rules are enforced.

1.3. High-technology sectors

- High-technology sectors, such as semiconductors, are highly R&D and capital intensive. Common forms of support are R&D subsidies as well as tax breaks or other investment incentives. While there are good economic arguments for supporting R&D, care should be taken to do so in a manner that maximises social benefits while minimising competitive distortions.
- Support provided through the financial system is again important – this time, below-market equity, which is even more challenging to measure and provides not simply a one-off benefit but also creates channels for the provision of other support in future. Tackling this support may require going beyond subsidy rules to devising specific rules on state enterprises and government-invested firms.
- While there is substantial state involvement and government support in the semiconductor value chain, there were also questions about whether this support actually works in terms of increasing innovation and productivity in R&D-intensive industries characterised by short product cycles. Yet however effective it is, the provision of large amounts of support can nevertheless cause significant trade distortions that are a serious concern.

1.4. Addressing market distorting government support

- Enhanced transparency is the number one priority and a precondition for enhanced disciplines to level the playing field and address market-distorting government support.
- There is a need to strengthen the WTO notification mechanisms, not only for government support, but also to increase transparency on the extent and nature of government investment in firms.
- Using multiple channels to enhance transparency is a useful approach. Data provided through OECD work can usefully complement the information obtained through existing WTO mechanisms.
- Building on transparency, effective subsidy disciplines also need to ensure predictability (that support will not increase); reduction (removal of the most egregious support, and disciplining other forms); and prevention (of tomorrow's subsidies in tomorrow's sectors).
- Given the general proliferation of government support, a possible way forward is to start focusing on the reduction of the most egregious forms of support.
- It was acknowledged that disciplines needed to go beyond subsidies to tackle the role of state enterprises or government-invested firms.

1.5. Ways forward

- There is an urgent need for tougher rules to discipline government support, along with strengthened WTO transparency mechanisms and enforcement.
- These issues should preferably be addressed at an international level because only global action can both address existing problems and prevent the emergence of new support in other sectors by

new players. A strong message at the WTO MC12 would be helpful. Long-term, sustainable solutions need to begin now.

- OECD work on government support will continue, potentially looking at additional sectors, as well as in more depth at specific types of support instruments across sectors.

1.6. Special session on digital trade and the "Osaka track"

- The WTO e-commerce discussions and the "Osaka track" are useful initiatives to develop a new regulatory policy framework on digital trade.
- Bilateral trade agreements contain provisions that have bearing on digital trade and could be useful reference points for ongoing discussions at the WTO.
- Continued efforts are needed to reduce the current patchwork of approaches to regulating cross-border data flows by looking at ways of making these more interoperable.
- OECD work on digital trade is a particularly useful contribution to WTO discussions and relevant dialogues domestically and in other international fora.
- These exchanges were seen as enabling the government and private sector representatives to shape common understandings and to exchange views, not only on the rules necessary in today's digital era, but also on how various international fora and organisations can contribute to rule-making.

2. Detailed summary record

The Global Forum on Trade started with an overview of OECD's evidence on government support, then moved to specific sectors including agriculture and industrial goods, namely the aluminium sector and the semiconductor value chain. Subsequently, the participants engaged in a country-led discussion on approaches to addressing government support for industrial goods, drew initial conclusions from the discussions, and exchanged views on possible ways forward for addressing trade-distorting measures. A special session on digital trade, including the "Osaka Track", discussed the progress under the WTO joint initiative on e-commerce, and provided an update on relevant OECD work.

2.1. What is the evidence on government support?

This session provided a broad overview of OECD work on measuring government support, focusing on the indicative matrix of support measures that the OECD has developed based on its extensive work across several key sectors – agriculture, fisheries, fossil fuels subsidies, export restrictions on key raw materials, and, more recently, industrial goods. The OECD matrix both guides data collection and provides a heatmap of government support measures that will vary in importance across countries, firms, and stages of the value chain, presenting illustrative but not exhaustive examples under broad headings. The matrix picks up various types of support measures and classifies them according to their transfer mechanism (in what form a transfer is made, e.g. direct transfer of funds, reduced taxes, transfers of private risk and liabilities to governments) and their formal incidence (to what the transfer is given, e.g. for knowledge like R&D, or to reduce the cost of intermediate inputs).

This session noted that, while government support through transfers can be identified and quantified relatively precisely (e.g. by looking at government budgets), the measurement of below-market borrowings and below-market equity is significantly more complex and less precise. These types of support tend not to be disclosed, requiring complex research efforts and measurement exercises, requiring varied assumptions to be made.

2.2. Agriculture

The session on agriculture focused on what is known about support to agriculture and the implications for priorities for reform.

As key findings of the OECD's flagship publication *Agricultural Policy Monitoring and Evaluation* show, total support to agriculture (including support to farmers, general services to the sector, and consumer subsidies) across the 53 countries covered averaged USD 705 billion (United States Dollars) per year during 2016-2018. Of the USD 530 billion provided annually in public support to farmers, about two-thirds was provided through measures that strongly distort farm business decisions - thereby distorting global agricultural production and trade. At the same time, some countries' trade policies lower domestic prices relative to international prices, thereby effectively taxing producers to the tune of USD 83 billion per year. The report also highlights that governments have an opportunity to adopt new policy approaches than can achieve their objectives more effectively and, at the same time, reduce international market distortions.

To reflect on how distorting agricultural support could be addressed, the participants looked at two examples of reform processes: Australia, as one of the countries with the lowest agricultural government support, and Switzerland, as a country with a relatively high level of support. In Australia's case, the discussion showed that moving away from distorting agricultural support can be achieved through a number of policy actions, which include: good planning and embedding of agricultural reforms into economy-wide reforms; broader macroeconomic reform and stability; removing tariffs; ensuring competitive neutrality; shifting government intervention from direct support to farmers to a sector-wide support and investment in research and development (e.g. digital and precision agriculture); and bringing along the farmers and support groups, as well as consumers.

The participants also discussed the example of Switzerland and its ongoing reform progress towards stronger market orientation and more targeted support, in particular the decoupling of support. The Swiss reforms of the sector were facilitated by external pressure, such as the outcomes of the Uruguay Round, enhanced calls for trade to contribute to sustainable development, and new social expectations.

The discussion highlighted that bringing stakeholders on board for agricultural reforms is particularly important and can be facilitated with active engagement and consultation processes. It is also important to communicate the benefits of reforms, and this can require engagement and efforts by political leaders.

Many participants agreed that there is potential for international co-operation and further agricultural reforms towards less trade-distorting government support, while recognising that progress has proved challenging and it can be challenging to identify low-hanging fruits in this area. Many Delegations called for WTO reforms to create external pressure for domestic processes. Some flagged that, while there are still substantial tariff barriers in some countries, it would be helpful to also reduce the "water in the tariffs" (where bound tariffs are significantly higher than those actually applied) in order to reduce policy uncertainty. Other speakers flagged that different issues needed to be linked and that it is important to achieve a balanced outcome overall. It was also pointed out that it was not possible to discuss government support in agriculture without also discussing the need to expand market access, which is also one of the big challenges in the context of the discussion in Geneva.

There was agreement on the usefulness of OECD's work on measuring agricultural support and its contribution to enhanced transparency in this area. The OECD was encouraged to continue analysing domestic support to better understand the consequences of these policies, identify better policies and exchange good practices, including on the political economy of reforms. A further emerging issue was agriculture in the context of sustainable development, and how to ensure that any support achieved its aims without distorting international markets. Some participants called for enhanced research on related border adjustments.

2.3. Aluminium

In this session, discussion with representatives of the aluminium industry focused on the main findings of the 2019 OECD report on "Measuring distortions in international markets: the aluminium value chain" and its implications for reform priorities.

Results in this report, which estimates government support and related market distortions along the aluminium value chain, show that non-market forces, and government support in particular, appear to explain some of the recent increases in aluminium-smelting capacity. Looking across the whole value chain shows subsidies upstream to confer significant support to downstream activities, such as the production of semi-fabricated products of aluminium. Additionally, state entities emerge as important providers – and not just recipients – of government support, notably through the financial system, in the form of below-market loans. The influence of the state also has implications for the transparency of support policies. Overall, market distortions appear to be a genuine concern in the aluminium industry, and one that has implications for global competition and the design of trade rules disciplining government support.

Participants shared their perspectives on the main challenges that government support creates for trade and competition in the aluminium sector. A key issue that emerged was the scale and nature of support, and its effect on competition in the sector and global aluminium prices. A serious issue throughout the value chain relates to support for cheap primary aluminium, which, combined with significant amounts of government support downstream, has enabled some producers of semi-fabricated products of aluminium to undercut competitors in this market. Many participants stressed the need for the global aluminium value chain to respond to market forces as opposed to government support, and to let market signals dictate success and failure. They also called for a global, co-ordinated policy response to ensure fair competition in the market, noting that clear rules are still missing and that the establishment of new rules will need to go hand-in-hand with a mechanism for continuous global enforcement.

The OECD report was commended for being impressively comprehensive, highly innovative and extremely valuable as it injected some much-needed transparency into government support in the aluminium markets. Going forward, the OECD was encouraged to look at those policy categories that are most highly market distorting, e.g. by focussing on a set of policies such as below market financing. This may allow the OECD to draw insights that cut across several sectors and apply more generally, thus helping anticipate areas of future risks before they materialise.

2.4. High-technology sectors: the semiconductor value chain

Discussion in this panel highlighted some of the specificities of government support in high-technology sectors, including support for research and development and support provided via equity injections.

The semiconductor industry is highly R&D-intensive, and much of the support provided from government budgets targeted R&D activities of semiconductor firms (e.g., through grants or tax breaks). While there can be good economic reasons for supporting R&D – such as correcting market failures – care should be taken to do so in a manner that maximises societal benefits (i.e., innovation) while minimising competitive distortions. This includes, for example, transparent and non-discriminatory policies that benefit either young firms that face financing constraints, or support for pre-competitive research.

Support provided through the financial system is again important – this time, below-market equity, which is even more challenging to measure and provides not simply a one-off benefit but also creates channels for the provision of other support in future. The issue of state ownership and government involvement in semiconductor production is also highly complex and increasingly difficult to tackle and there is a need for much greater transparency on the extent of government investment in semiconductor firms. Tackling this support may require going beyond subsidy rules to devising specific rules on state enterprises and government-invested firms.

While there is substantial state involvement and government support in the semiconductor value chain, there were questions about whether this support actually works in terms of increasing innovation and productivity in R&D-intensive industries characterised by short product cycles given the important role of learning by doing and intangible knowledge. There were two schools of thought: those who felt that such support had not resulted in recipients reaching cutting edge technology (although they may enjoy strong market positions in other sub-sectors), and others who felt that the nature and scale of support had significantly increased in recent times and that its results were yet to be felt. Yet however effective it is, the provision of large amounts of support can nevertheless cause significant trade distortions that are a serious concern.

There was broad agreement on the need to enhance transparency on government support. It was regretted that the WTO transparency obligations have not been respected and much government support has not been notified. The implementation and enforcement of transparency obligations were therefore considered as a top priority for action. Discussion was also needed on how to ensure that subsidy rules could be effective in real time, especially for high technology sectors. Currently, it takes too much time to bring a case before the WTO, and the enforceable action comes too late, and is too weak, while the damage has already occurred.

2.5. Addressing market distortions to industrial goods

Based on the discussion in the previous sessions, this session was led by countries and explored approaches to addressing key areas for strengthening disciplines on industrial support. There was general agreement that existing WTO rules were struggling to discipline some of the new forms and scale of government support.

Participants highlighted that industrial sectors are increasingly facing competition that is receiving significant government support. Increasing levels of trade-distorting support channelled through state enterprises make it particularly difficult to determine what support is being received and whether firms are operating on the basis of commercial practices. The proliferation of below-market financing (both cheap loans and below market equity) in particular is extremely difficult both to measure and to capture under existing WTO rules. Additionally, the cumulative effect of support along the value chain was also not well captured by the current rules.

There was discussion about the priorities for reform. Enhancing transparency was universally considered a top priority action for addressing market-distorting government support. There is a need to strengthen the WTO notification mechanism, given the high level of non-compliance with notification obligations. Some Delegations noted that there was currently no penalty for non-notification and supported proposals to introduce a range of consequences for non-notification. Others noted that it could be useful to draw on multiple channels to enhance transparency – for example, by drawing on data provided through OECD work to complement the information obtained through existing WTO mechanisms (notifications, counter-notifications, and the WTO Trade Policy Review). While transparency provisions have increasingly been included in recent bilateral agreements, some Delegations noted that this is a global trade issue and should be covered by global rule making. Lastly, transparency should cover not only government support, but also the extent and nature (e.g., golden share, appointment of Board members) of government investment in firms.

Beyond transparency, effective subsidy disciplines also need to ensure predictability (that support will not increase); reduction (removal of the most egregious support, and disciplining other forms); and prevention (of tomorrow's subsidies in tomorrow's sectors). There were a number of calls to focus first on prohibiting the most distorting subsidy types, as well as seeking to put stronger disciplines on relatively more distorting support ("dark amber" support). There was some discussion about the ways in which support could be disciplined and some of the challenges of burden of proof addressed. Moreover, it was acknowledges that disciplines needed to go beyond subsidies to tackle the role of state enterprises or government-invested firms. There was also some discussion about the absence of rules on services, and the role that increasing servicification of manufacturing could play in this regard.

2.6. Ways forward for addressing trade-distorting practices

This session drew initial conclusions from the day in terms of priorities and possible ways forward for addressing government support.

A key conclusion was that the measurement of government support is highly important, in particular as governments make growing use of forms of subsidies that are difficult to capture, e.g. below-market financing. Thanks to the OECD there is now in some sectors a better understanding of the kind of measures that are being increasingly used and that are having a distorting effect.

There was also general agreement on the need for enhanced transparency on government support. It is important to gather robust information on the type and amount of support firms are receiving. It was critical to strengthen WTO notifications, but also to draw on different channels, with an important role for the analysis and measurement undertaken by the OECD. OECD work on government support will continue, potentially looking at additional sectors, as well as in more depth at specific types of support instruments across sectors.

There was considerable interest in the need for tougher subsidies rules and strengthened WTO mechanisms and enforcement. Only global action could both address existing problems and prevent the emergence of new support in other sectors by new players. A strong message at the WTO MC12 would be helpful. Long-term, sustainable solutions needed to begin now.

2.7. SPECIAL SESSION: Digital Trade, including the "Osaka Track"

In this special session, participants discussed the state of play of the debate on digital trade, including the "Osaka Track".

The session began with a keynote speech from Mr. Shuji Miyamoto, Parliamentary Vice-Minister of Japanese Ministry of Economy, Trade and Industry. The Vice-Minister outlined the "Osaka Track", the process on international policy discussions on digital economy which was affirmed by Leaders participating in the Osaka Declaration on Digital Economy in June 2019, as a series of multi-stakeholder dialogues to i) foster common understanding among the WTO Members participating in the ongoing WTO e-commerce discussions with a view to achieve substantial progress by MC12; ii) making best use of expertise from the OECD and other international fora in addition to the WTO; and iii) promoting holistic policy discussions on digital economy, not limited to those covered under the WTO discussions. As a particular example of the element beyond the scope of WTO e-commerce discussions, Mr. Miyamoto referred to various relevant analytic work on digital trade and the ongoing work on governance innovation by the OECD, i.e. regulatory reform in the digital era.

During the session, an update on the WTO E-commerce discussions highlighted the broad range of issues covered, including: market access; trade facilitation for goods and services; *de minimis* thresholds; trade in services; data flows; data localisation; commitments on transparency; consumer protection; and privacy. The discussions of the Joint Statement Initiative in September focused on streamlined texts, merging text from different proposals. Another round of discussions in November would cover data flows, data localisation, source codes, customs duties on electronic transmissions, capacity building and trade facilitation. These discussions continue to be constructive and involve a high degree of engagement, especially in the run up to the WTO MC12 in June 2020.

The WTO e-commerce discussions and the "Osaka track" were welcomed as useful initiatives to help develop a new regulatory policy framework on digital trade. Also highlighted was the importance of bilateral trade agreements such as the USMCA, the CPTPP and the EU-Japan agreement, which contain provisions that have bearing on digital trade and which could be useful reference points for ongoing

discussions at the WTO. The recent negotiations for Chile, Singapore and New Zealand digital economy partnership, which goes beyond traditional trade disciplines and undertakes to consider all aspects of the digital economy, was also mentioned.

The discussion involving private sector representatives revealed the importance of cross-border data flows for global businesses. However, governments are increasingly imposing a range of differing conditions on cross-border data flows and/or requiring that data be stored in local servers (data localization). Calls were made for continued efforts to reduce the current patchwork of approaches by looking at ways of making these more interoperable. Highlighted proposals included: i) prohibition of local data storage and processing requirements, ii) making permanent the WTO moratorium on customs duties on electronic transmissions, iii) risk-based, interoperable and technology-neutral cybersecurity and data privacy regimes, and iv) encouraging private sector initiatives on best practices and codes of conduct.

The need for regulatory coherence and for minimising unnecessary regulatory divergence was also emphasised, as was the need for enhanced consultation with the private sector. Private sector participations also highlighted the importance of standards in the areas of cybersecurity and AI, where the standards need to keep up with the technology. There were also calls for a ban of forced disclosure of source codes.

The OECD was congratulated for its work on digital trade, which was considered a useful contribution to WTO discussions and to relevant dialogues domestically and in other international fora. The OECD paper on the Moratorium was praised as particularly timely and useful to the ongoing discussions. Highlighted was also relevant work on trade and cross border data flows, which looks into governments' approaches to data flow regulations; the digital STRI; work on trade in parcels; and work on how SMEs can benefit from and participate in digital trade. Going forward, the aim is to continue building knowledge on digital trade related issues but also to increasingly apply this expertise to specific country contexts. TAD will also continue to contribute to the OECD's Going Digital initiative, which represents a whole of society approach, looking into issues such as blockchain and the well-being dimension. The OECD Principles on Artificial Intelligence were flagged as a particularly relevant contribution, which was used also in the G20 process.

Several participants stressed the value of continuing a dialogue such as the one at this Global Forum on Trade. These exchanges enable government and private sector representatives to shape common understandings and to exchange views, not only on the rules necessary in today's digital era, but also on how various international fora and organisations can contribute to rule-making.