

## ANNEX II

**GUIDELINES ON CONSUMPTION OF  
INPUTS IN THE PRODUCTION PROCESS<sup>(1)</sup>**

1. Indirect tax rebate schemes can allow for exemption, remission or deferral of prior-stage cumulative indirect taxes levied on inputs that are consumed in the production of the exported product (making normal allowance for waste). Similarly, drawback schemes can allow for the remission or drawback of import charges levied on inputs that are consumed in the production of the exported product (making normal allowance for waste).
2. The illustrative list of export subsidies in Annex I makes reference to the term ‘inputs that are consumed in the production of the exported product’ in points (h) and (i). Pursuant to point (h), indirect tax rebate schemes can constitute an export subsidy to the extent that they result in exemption, remission or deferral of prior-stage cumulative indirect taxes in excess of the amount of such taxes actually levied on inputs that are consumed in the production of the exported product. Pursuant to point (i), drawback schemes can constitute an export subsidy to the extent that they result in a remission or drawback of import charges in excess of those actually levied on inputs that are consumed in the production of the exported product. Both points stipulate that normal allowance for waste must be made in findings regarding consumption of inputs in the production of the exported product. Point (i) also provides for substitution, where appropriate.
3. In examining whether inputs are consumed in the production of the exported product, as part of a countervailing duty investigation pursuant to this Regulation, the Commission must normally proceed on the following basis.
4. Where it is alleged that an indirect tax rebate scheme, or a drawback scheme, conveys a subsidy by reason of over-rebate or excess drawback of indirect taxes or import charges on inputs consumed in the production of the exported product, the Commission must normally first determine whether the government of the exporting country has in place and applies a system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts. Where such a system or procedure is determined to be applied, the Commission must normally then examine the system or procedure to see whether it is reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export. The Commission may deem it necessary to carry out, in accordance with Article 26(2), certain practical tests in order to verify information or to satisfy itself that the system or procedure is being effectively applied.
5. Where there is no such system or procedure, where it is not reasonable, or where it is instituted and considered reasonable but is found not to be applied or not to be applied effectively, a further examination by the exporting country based on the actual inputs involved will normally need to be carried out in the context of determining whether an excess payment occurred. If the Commission deems it necessary, a further examination may be carried out in accordance with point 4.
6. The Commission must normally treat inputs as physically incorporated if such inputs are used in the production process and are physically present in the product exported. An input need not be present in the final product in the same form in which it entered the production process.

7. In determining the amount of a particular input that is consumed in the production of the exported product, a 'normal allowance for waste' must normally be taken into account, and such waste must normally be treated as consumed in the production of the exported product. The term 'waste' refers to that portion of a given input which does not serve an independent function in the production process, is not consumed in the production of the exported product (for reasons such as inefficiencies) and is not recovered, used or sold by the same manufacturer.
8. The Commission's determination of whether the claimed allowance for waste is 'normal' must normally take into account the production process, the average experience of the industry in the country of export, and other technical factors, as appropriate. The Commission must bear in mind that an important question is whether the authorities in the exporting country have reasonably calculated the amount of waste, when such an amount is intended to be included in the tax or duty rebate or remission.

- (1) Inputs consumed in the production process are inputs physically incorporated, energy, fuels and oil used in the production process and catalysts which are consumed in the course of their use to obtain the exported product.