ANNEX A

FIRST WRITTEN SUBMISSIONS OF PARTIES AND THIRD PARTIES

ANNEX A-1

EXECUTIVE SUMMARY OF THE FIRST WRITTEN SUBMISSION OF BRAZIL

(Executive summary submitted on 24 November 2006)

1. This dispute results from the United States' failure to implement, in a timely and complete manner, the recommendations and rulings of the Dispute Settlement Body ("DSB") in *U.S. – Upland Cotton*. Brazil challenges both the *existence* and *consistency* of U.S. measures taken to comply with the "adverse effects"- and "export credit guarantee"-related recommendations and rulings of the DSB.

BRAZILIAN CLAIMS CONCERNING ADVERSE EFFECTS-RELATED RECOMMENDATIONS AND RULINGS OF THE DSB

2. In its adverse effects-related recommendations and rulings, the original panel, as affirmed by the Appellate Body, found that the price-contingent U.S. marketing loan program, counter-cyclical payment program and Step 2 program of the FSRI Act of 2002 caused significant price suppression in the world market for upland cotton, in violation of Articles 5(c) and 6.3(c) of the *Agreement on Subsidies and Countervailing Measures* ("*SCM Agreement*"). The panel found that "the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice findings."[1] The Dispute Settlement Body adopted the panel and Appellate Body reports that obliged the United States to remove the adverse effects caused by the subsidies, or to withdraw the subsidies, by 21 September 2005.

3. The United States did not repeal or amend any of the three price-contingent subsidy programs until 1 August 2006, when it finally discontinued solely the Step 2 program. The far larger marketing loan and counter-cyclical payment programs have not been removed or amended to this day. Brazil asserts four claims related to adverse effects implementation.

4. ***First***, Brazil claims that between the expiry of the implementation period on 21 September 2005 and elimination of Step 2 payments on 1 August 2006, there did not "exist" any U.S. "measures taken to comply" with the adverse effects-related recommendations and rulings of the DSB.[2]

5. ***Second,*** Brazil claims that the non-repealed price-contingent U.S. marketing loan and counter-cyclical payment programs cause present serious prejudice in the form of significant price suppression in the world market for upland cotton, and an increase in the U.S. world market share, in violation of Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*. In other words, Brazil claims that, to the extent measures taken to comply with the adverse-effects related recommendations and rulings of the DSB exist (*i.e.*, the repeal of Step 2 and the non-repeal of the marketing loan and counter-cyclical payment programs), those measures continue to result in inconsistencies with the covered agreements, within the meaning of Article 21.5 of the DSU.[3]

6. Brazil establishes serious prejudice to its interests based on data for the most recently completed marketing year ("MY") – MY 2005. Full-year data on marketing loan and counter-cyclical payments to U.S. upland cotton farmers for MY 2006 – the first year in which Step 2 is not provided –

[1] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.
[2] *See* Section 6 of Brazil's First Written Submission.
[3] *See* Section 7 of Brazil's First Written Submission.

will not be available until September 2007. Nevertheless, the compliance Panel, like the original panel, can use a counter-factual analysis to evaluate the effects of marketing loan and counter-cyclical payments alone, and factor out any additional effects of Step 2 (or other subsidy) payments made in MY 2005.

7. As a preliminary step, Brazil establishes that the marketing loan and counter-cyclical payment programs of the FSRI Act of 2002 constitute subsidies that are specific, within the meaning of Articles 1 and 2 of the *SCM Agreement*.[4] In addition, upland cotton from Brazil continues to be a like product with subsidized U.S. upland cotton and there continues to be a world market and the A-index continues to constitute the world market price for upland cotton.[5]

8. To demonstrate a causal link between U.S. marketing loan and counter-cyclical payments and significant price suppression, within the meaning of Article 5(c) and 6.3(c) of the *SCM Agreement*, Brazil examines the same factors relied upon by the original panel.

9. As the largest exporter of upland cotton in the world, the United States remains the single most important market influencing world market prices. Changes in the volume of U.S. production, carry-over stocks, and exports have a significant impact on world market prices.[6] In addition, movements in U.S., Brazilian, A-Index and futures market prices continue to show a broad similarity and remain low relative to long term averages.[7]

10. The magnitude of marketing loan and counter-cyclical payments in MY 2005 was massive, amounting to $2.17 billion, or 42 percent of the market value of U.S. upland cotton production.[8] As the original panel found, the structure, design and operation of these subsidies continue to insulate U.S. upland cotton producers from market forces[9], leading to high levels of U.S. planted acreage, production and exports and, ultimately, suppressed world market prices.[10] Thus, there remains a discernable temporal coincidence between these subsidies and suppressed world market prices.[11]

11. Over the long term (six years), U.S. costs of production for upland cotton continue to greatly exceed market revenues. Without subsidies, the average acre planted to upland cotton between MY 2000-2005 would have lost $663, or $9.84 billion for all acres. However, when revenue from marketing loan and counter-cyclical payments is included with market revenue, the average acre would have made a total six-year profit of $127, or $1.44 billion in aggregate. These facts succinctly demonstrate that the effect of marketing loan and counter-cyclical payments is to sustain higher levels of output than would otherwise exist.[12]

12. Economic studies by leading academics show that marketing loan and counter-cyclical payments continue to stimulate U.S. production and exports and result in lower world market prices than would prevail in their absence. Professor Daniel Sumner finds that the world market price of upland cotton would have been between 9 and 11 percent higher in MY 2005 in the absence of these two U.S. subsidy programs.[13]

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[4] *See* Section 7.3 of Brazil's First Written Submission.
[5] *See* Section 7.4 of Brazil's First Written Submission.
[6] *See* Section 7.5 of Brazil's First Written Submission.
[7] *See* Section 7.6 of Brazil's First Written Submission.
[8] *See* Section 7.7 of Brazil's First Written Submission.
[9] *See* Section 7.8 of Brazil's First Written Submission.
[10] *See* Section 7.9 of Brazil's First Written Submission.
[11] *See* Section 7.10 of Brazil's First Written Submission.
[12] *See* Section 7.11 of Brazil's First Written Submission.
[13] *See* Section 7.12 of Brazil's First Written Submission.

13. In view of the size and nature of U.S. upland cotton subsidies and the commanding U.S. market share, the price suppression is unmistakably significant.[14] Any price-suppressing effects of Step 2 payments do not diminish the significant and independent price-suppressing effects of marketing loan and counter-cyclical payments. Indeed, the U.S. Congressional Budget Office concludes that counter-cyclical payments will be even larger in the absence of Step 2 payments. [15] Similarly, other non-subsidy factors that impact the world market price of upland cotton do not account for the price suppression caused by marketing loan and counter-cyclical payments.[16]

14. Brazil also claims that the U.S. marketing loan and counter-cyclical payments cause serious prejudice to the interests of Brazil by increasing the U.S. share of the world upland cotton market, within the meaning of Article 5(c) and 6.3(d) of the *SCM Agreement*. The U.S. world market share of upland cotton increased from an average of 19.32 percent in MY 2002-2004 to 20.85 percent in MY 2005, or from 16.98 percent in MY 2002-2004 to 17.44 percent in MY 2005, depending on approach used to measure supply. The same effects from marketing loan and counter-cyclical payments that stimulate excessive U.S. production and exports and lower world market prices – despite high costs and low market revenue and prices – also causes the increase in U.S. world market share.[17]

15. In sum, Brazil requests the compliance Panel to find that the U.S. measure eventually taken to comply, *i.e.*, the amendment of the FSRI Act of 2002 to repeal Section 1207(a), providing for Step 2 payments, is insufficient to ensure compliance with the recommendations and rulings of the DSB, because the resulting basket of measures is inconsistent with Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*.

16. ***Third,*** Brazil claims that despite the repeal of the Step 2 program, the marketing loan and counter-cyclical payments mandated under the FSRI Act of 2002 to be made in MY 2006, and beyond, cause a *threat* of serious prejudice to the interests of Brazil, within the meaning of Articles 5(c) and 6.3(c), as well as footnote 13 of the *SCM Agreement*. Brazil again claims that, to the extent measures taken to comply with the adverse-effects related recommendations and rulings of the DSB exist (*i.e.*, the repeal of the Step 2 program and the non-repeal of the marketing loan and counter-cyclical payment programs), those measures are deficient, and result in inconsistencies with the covered agreements, within the meaning of Article 21.5 of the DSU. Brazil notes that this claim is contingent on the compliance Panel not being able to find that the marketing loan and counter-cyclical payment programs cause present serious prejudice (Brazil's second adverse effects-related claim).

17. Key evidence supporting Brazil's threat claim includes the fact that the two remaining subsidy programs – the marketing loan and counter-cyclical payment programs – are mandatory, result in guaranteed high levels of U.S. planted acreage, production and exports and have caused significant price suppression throughout the history of the FSRI Act of 2002. With the repeal of the Step 2 program and the resulting lower *domestic* market prices in the United States, the effects of the remaining two price-contingent U.S. subsidy programs will be, if anything, bigger in MY 2006, and beyond. In fact, USDA and FAPRI projections regarding U.S. subsidy outlays under these programs, upland cotton production, exports, prices and developments in U.S. cost of production for upland cotton support a finding of a threat of serious prejudice from the U.S. marketing loan and counter-cyclical payments for upland cotton. These two subsidy programs under the FSRI Act of 2002 constitute a continuing threat of significantly suppressed world market prices for Brazilian and other developing country producers that will continue until these measures are repealed or significantly

[14] *See* Section 7.13 of Brazil's First Written Submission.
[15] *See* Section 7.14 of Brazil's First Written Submission.
[16] *See* Section 7.15 of Brazil's First Written Submission.
[17] *See* Section 7.17 of Brazil's First Written Submission.

amended. Indeed, these subsidies caused serious prejudice during the first four years of the FSRI Act of 2002, continue to cause present serious prejudice, and continue to cause a threat thereof.[18]

18. ***Fourth*****,** Brazil claims, on a contingent basis, that during the period 21 September 2005 to 31 July 2006, all three of the price-contingent subsidy programs of the FSRI Act of 2002, mentioned above, have caused serious prejudice to Brazil. Brazil requests that the compliance Panel address this claim only if it rejects Brazil's first, second and third claim, as outlined above. Brazil claims that the failure of the United States to take any measures to remove the adverse effects or withdraw the three price-contingent subsidy programs during this period has caused serious prejudice to the interests of Brazil, in violation of Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*.[19]

19. In sum, with respect to the adverse effects-related recommendations and rulings of the DSB, Brazil requests the compliance Panel to conclude that the original recommendation adopted by the DSB – to "remove the adverse effects or [to] the subsidy" under Article 7.8 of the *SCM Agreement* – remains in effect, and applies to the full extent of the findings requested by Brazil in these Article 21.5 proceedings.[20]

BRAZILIAN CLAIMS CONCERNING EXPORT CREDIT GUARANTEE-RELATED RECOMMENDATIONS AND RULINGS OF THE DSB

20. The DSB recommended that the United States withdraw the three export credit guarantee ("ECG")subsidies maintained by the U.S. Commodity Credit Corporation ("CCC") – the GSM 102, GSM 103 and SCGP programs – and otherwise bring itself into compliance with its obligations by the implementation deadline of 1 July 2005. To implement the DSB's recommendations and rulings, the United States announced, on 1 July 2005, that CCC would no longer take applications for ECGs under GSM 103, which underwrote credit for 3- to 10-year periods, and amended the fee schedules for ECGs issued under the GSM 102 and SCGP programs.[21] Brazil raises two claims with respect to the U.S. measures taken to comply with the ECG-related recommendations and rulings of the DSB.

21. ***First***, with respect to ECGs issued under the GSM 102, GSM 103 and SCGP programs prior to 1 July 2005, but still outstanding subsequent to 1 July 2005, the United States has taken no action whatsoever to withdraw the subsidy and otherwise bring itself into conformity with its obligations. In regard to these outstanding ECGs, Brazil claims that measures taken to comply do not exist.[22]

22. ***Second***, with respect to ECGs issued subsequent to 1 July 2005, they continue to be export subsidies, and continue to be provided in a manner that results in circumvention of the United States' export subsidy commitments. In this regard, the United States' measures taken to comply are not consistent with Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*.[23]

23. Since 1 October 2005 – the beginning of FY 2006 – the United States has not issued any SCGP ECGs. Nor have any GSM 103 ECGs been issued since 1 July 2005, the implementation deadline. Thus, Brazil's second claim, of continued inconsistency with the *Agreement on Agriculture* and the *SCM Agreement*, applies solely to GSM 102, and not to GSM 103 or SCGP.[24]

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[18] *See* Section 8 of Brazil's First Written Submission.
[19] *See* Section 9 of Brazil's First Written Submission.
[20] *See* Section 10.3.3 of Brazil's First Written Submission.
[21] *See* Section 10.2 of Brazil's First Written Submission.
[22] *See* Section 10.3.1 of Brazil's First Written Submission.
[23] *See* Section 10.3.2 of Brazil's First Written Submission.
[24] *See* Section 10.3.2 of Brazil's First Written Submission.

24. GSM 102 ECGs guarantee the repayment of credit made available to finance commercial exports of U.S. agricultural products. The guarantees cover 98 percent of the principal and a portion of the interest, and have a duration of 30 days to three years. GSM 102 operates solely in circumstances where a foreign bank could not, without the U.S. government's assistance, secure the credit necessary to on-lend to its customer, the purchaser of U.S. agricultural exports.[25]

25. Using the context of Articles 1 and 3.1(a) of the *SCM Agreement*, GSM 102 ECGs constitute export subsidies for the purposes of Article 10.1 of the *Agreement on Agriculture*. Specifically, GSM 102 ECGs (i) are "financial contributions" (ii) that confer "benefits", and (iii) are contingent in law on export performance.[26]

26. With respect to the *first element*, Article 1.1(a)(1)(i) of the *SCM Agreement* includes as a "financial contribution" "potential direct transfers of funds or liabilities (*e.g.* loan guarantees)." GSM 102 ECGs fall squarely within this definition. The *third element* is similarly straightforward. Article 3.1(a) of the *SCM Agreement* prohibits "subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance …." GSM 102 ECGs are expressly conditioned on the export of eligible U.S. agricultural products.[27]

27. Turning to the *second element*, Article 1.1(b) of the *SCM Agreement* provides that a "benefit" must be conferred by virtue of the financial contribution. The appropriate standard for determining the existence of a benefit is whether the financial contribution has left the recipient better off than it would otherwise have been. In the case of loan guarantees, panels have adopted two approaches to applying this standard. Under either approach, GSM 102 and GSM 102 ECGs are provided on terms that constitute "benefits."[28]

28. The first approach seeks to determine whether the government guarantee improves the terms of the underlying loan compared to the terms that could have been secured without the government guarantee. This approach builds on the benefit valuation principle in Article 14(c) of the *SCM Agreement*. Article 14(c) calls for an examination focused on the difference between the amount paid on a loan guaranteed by the government, compared to the amount that would have to be paid on a comparable commercial loan, absent the government guarantee. Article 14(c) presumes, of course, that a commercial loan could be secured by a recipient in the absence of the government guarantee. If *no loan* would be available without the government guarantee – as U.S. regulations establish is the case with transactions covered by the GSM 102 program – a benefit exists *per se*. This is in keeping with Article 1.1(b) of the *SCM Agreement*, because if a "financial contribution" enables the recipient to obtain a commercial loan that could not be otherwise obtained, an advantage beyond what is available in the marketplace, or in other words, a "benefit", is conferred.[29]

29. The second approach builds on Article 1.1(b) of the *SCM Agreement*, and seeks to determine whether the government guarantee is available on terms better than a market-based guarantee.[30] Brazil compares GSM 102 fees with fees for comparable instruments offered by the Export-Import Bank of the United States ("ExIm Bank"), the official export credit agency of the United States. Although ExIm bank is not a commercial operator, and indeed, assumes risk the private sector is unable or unwilling to assume, the exercise offers a useful set of comparison points. Of the 1071 comparison points generated by the benchmarking exercise, GSM 102 fees were below comparable ExIm Bank fees 98 percent of the time. ExIm Bank fees exceeded GSM 102 fees by an

[25] *See* Section 10.3.2.1 of Brazil's First Written Submission.
[26] *See* Section 10.3.2.2 of Brazil's First Written Submission.
[27] *See* Section 10.3.2.2.1 of Brazil's First Written Submission.
[28] *See* Section 10.3.2.2.1 of Brazil's First Written Submission.
[29] *See* Section 10.3.2.2.1.1 of Brazil's First Written Submission.
[30] *See* Section 10.3.2.2.1.2 of Brazil's First Written Submission.

average of 112 percent for transactions involving annual repayment of principal, and 97 percent for transactions involving semi-annual repayment of principal. Accordingly, by comparison with fees charged by ExIm Bank for comparable products, GSM 102 ECGs provide a considerable "benefit," under Article 1.1(b) of the *SCM Agreement*.[31]

30. A further examination of GSM 102 ECGs shows that they are not *designed* to charge fees that are consistent with market. The CCC does not take account of the full costs of all of the risks it bears in a GSM 102 transaction. In fact, by USDA's own admission, CCC is unable to do so given the one-percent fee cap mandated by U.S. law. The CCC is limited by the program's structure and design from taking full account of the risks that would be factored into pricing decisions by market-based guarantors. It is, therefore, no surprise that the fees for GSM 102 ECGs are provided on terms better than could be secured by recipients were they to look for similar protection in the market.[32]

31. In sum, using the context of Articles 1 and 3.1(a) of the *SCM Agreement*, GSM 102 ECGs constitute export subsidies for the purposes of Article 10.1 of the *Agreement on Agriculture*.

32. Brazil notes that in the original proceedings, both the panel and the Appellate Body relied on the context offered by item (j) of the Illustrative List to inform the interpretation of the term "export subsidies" in Article 10.1 of the *Agreement on Agriculture*. As was the case before the original panel, GSM 102 fees continue to be insufficient to cover the long-term operating costs and losses of the program.[33] Brazil requests that the compliance Panel only consider this alternative claim under item (j) if it finds that GSM 102 ECGs are not export subsidies by virtue of the fact that they are "financial contributions" that confer "benefits" and that are export contingent, under Articles 1.1 and 3.1(a) of the *SCM Agreement*.

33. Although GSM 102 ECGs issued in Fiscal Years (FY) 2006 and 2007 are subject to the amended GSM 102 fee schedule, the United States nevertheless projects that the CCC will suffer losses by the time the 2006 and 2007 "cohorts" – or class of GSM 102 ECGs issued in those years – close. Specifically, CCC projects losses of USD 125 million and USD 114 million, respectively, for GSM 102 ECGs issued in FY 2006 and FY 2007 (before accounting for the costs of administering the program). In other words, the United States itself does not believe that the new GSM 102 fee schedule will result in income sufficient to absorb total losses incurred on the ECGs to which that fee schedule applies.

34. Brazil notes, moreover, that fees for GSM 102 ECGs fall below the minimum premium rates ("MPRs") provided in the Organization for Economic Co-operation and Development's ("OECD") Arrangement on Officially Supported Export Credits (the "Arrangement"). Brazil calculates 1064 comparison points between GSM 102 fees and MPRs. In 1063 of those 1064 comparisons, GSM 102 fees fall below the Arrangement's MPRs. The Arrangement's MPRs are on average 106 percent greater than GSM 102 fees, meaning that GSM 102 fees are strikingly "inadequate to cover long-term operating costs and losses associated with the provision of export credits".

35. Finally, for the same reasons indicated in the previous "benefit" analysis (see paragraph 30), Brazil contends that the structure, design and operation of the GSM 102 program under its amended fee schedule are such that fees remain inadequate to cover long-term operating costs and losses.

36. Having shown that GSM 102 ECGs are export subsidies, Brazil demonstrates that the United States has applied these export subsidies in a manner that results in circumvention of its export subsidy commitments. Brazil demonstrates that circumvention has occurred with respect to all

[31] *See* Section 10.3.2.2.1.2.1 of Brazil's First Written Submission.
[32] *See* Section 10.3.2.2.1.2.2 of Brazil's First Written Submission.
[33] *See* Section 10.3.2.2.2 of Brazil's First Written Submission.

unscheduled products and three scheduled products – rice, pig meat and poultry meat – in violation of Article 10.1 of the *Agreement on Agriculture*.[34]

37. In sum, Brazil demonstrates that the GSM 102 program, as maintained by the United States subsequent to 1 July 2005, is inconsistent with the *Agreement on Agriculture*. As a result, the United States is not due the full protection of the safe harbor accorded by the exception in the opening clause of Article 3.1 of the *SCM Agreement*, and the prohibition in Articles 3.1(a) and 3.2 applies.[35]

38. For the same reasons that the GSM 102 program and GSM 102 ECGs constitute export subsidies under the *Agreement on Agriculture*, they similarly constitute prohibited export subsidies under Articles 3.1(a) and 3.2 of the *SCM Agreement*. Brazil requests that the compliance Panel so find.

39. In sum, with respect to the ECG-related recommendations and rulings of the DSB, Brazil requests the compliance Panel to conclude that the original recommendation adopted by the DSB – to "withdraw the subsidy without delay" under Article 4.7 of the *SCM Agreement* – remains in effect, and applies to the full extent of the findings requested by Brazil in these Article 21.5 proceedings.[36]

[34] *See* Section 10.3.2.3 of Brazil's First Written Submission.
[35] *See* Section 10.3.3 of Brazil's First Written Submission.
[36] *See* Section 10.3.3 of Brazil's First Written Submission.

ANNEX A-2

EXECUTIVE SUMMARY OF THE FIRST WRITTEN SUBMISSION AND REQUEST FOR PRELIMINARY RULINGS OF THE UNITED STATES

(Executive Summary submitted on 22 December 2006)

1. The United States requests that the Panel reject Brazil's claims and find that the United States has complied with the DSB's recommendations and rulings and, further, that the U.S. measures taken to comply are not inconsistent with the *SCM Agreement* or the *Agreement on Agriculture*. The Step 2 program for users and exporters of U.S. cotton, worth *hundreds of millions of dollars* annually, was not the only program that the United States ceased to operate. It also ceased issuing guarantees under two export credit guarantee programs, namely, the GSM 103 program and the Supplier Credit Guarantee Program ("SCGP") program, under which the United States had been issuing applications for guarantees covering *hundreds of millions of dollars* of export transactions; the United States now issues *no* guarantees under either of the two programs. The third export credit guarantee program at issue in the underlying proceeding, the GSM 102 program, has been substantially modified and does not constitute an export subsidy. Further, the United States requests the Panel to make a preliminary ruling (as explained below) that certain measures and claims relating to export credit guarantees are not within the scope of this proceeding.

2. With respect to the Dispute Settlement Body's ("DSB") recommendations and rulings on actionable subsidies, the panel's finding of "present" serious prejudice in the original proceeding applied to a package of *payments* made under the Step 2, marketing loan, and counter-cyclical payment programs in marketing years ("MY")1999-2002. Those *payments* were, thus, the only measures subject to the DSB's recommendation under Article 7.8 of the *SCM Agreement* that the United States "take appropriate steps to remove the adverse effects or . . . withdraw the subsidy." Brazil submits no evidence whatsoever as to the present effects, if any, of the payments that were subject to the original panel's finding and thus appears to concede that these payments no longer have any effect. The United States requests the Panel to make preliminary rulings (as explained below) that certain measures and claims relating to certain U.S. *programs* are not within the scope of this proceeding. Without prejudice to those requests, the United States demonstrates that Brazil's claims with respect to U.S. programs also fail to withstand scrutiny.

3. **Export credit guarantees – GSM 102 guarantees have been provided subsequent to 1 July 2005 consistently with U.S. WTO obligations.** Brazil fails to make a *prima facie* case that GSM 102 export credit guarantees were provided subsequent to 1 July 2005 in a manner inconsistent with Articles 3.1 and 3.2 of the *SCM Agreement.* Article 3.1(a) of the *SCM Agreement* prohibits "subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I." Item (j) of the Illustrative List of Export Subsidies in Annex I "illustrates" or "makes clear" the conditions under which export credit guarantees may be considered export subsidies within the meaning of Article 3.1(a). Item (j) was the basis of the DSB's recommendations and rulings with respect to the U.S. export credit guarantee programs and, thus, it was the provision of the *SCM Agreement* that provided guidance to the United States in determining how to implement the DSB's recommendations and rulings. Item (j) is also the item that most directly addresses the issue in this dispute. Accordingly, in this case, it is item (j) that provides the basis for assessing whether or not GSM 102 export credit guarantees are export subsidies within the meaning of Articles 3.1(a) and 3.2 of the *SCM Agreement*.

4. The approach advocated by Brazil – to assess whether GSM 102 guarantees are export subsidies within the meaning of item (j) in the "alternative," only if the Panel finds that they are not 'financial contributions' that confer 'benefits' and that are export contingent under Articles 1.1 and 3.1(a) of the *SCM Agreement* – would lead to the fatally flawed result that a measure that was specifically found to fall *outside* the definition of an export subsidy could then be found to be an export subsidy.

5. In addition to ceasing to issue guarantees under the GSM 103 and SCGP, the United States has taken a number of steps to ensure that the graduated risk-based fee structure of the GSM 102 program covers the program's long-term operating costs and losses. Fees for the program now increase with both risk category and tenor (the length of the loan). The United States also reclassified into an ineligible risk category a large number of countries previously eligible under the programs. These changes made to implement the DSB's recommendations and rulings bolster other disciplines already in place.

6. The U.S. budget accounting data that has become available since the original proceeding show that, for all programs, for the fourteen-year period commencing with fiscal year 1992, the export credit guarantee programs received hundreds of millions of dollars more in premia and interest than required to pay out in operating costs and losses, including interest. These numbers indicate that the United States earned a substantial *profit* on its programs *even under the fee structure preceding the changes implemented on July 1, 2005*. With respect to the GSM 102 program, alone, the budget data also reflects that for every fiscal year cohort since 1992 the net lifetime re-estimates have been negative. Given that the programs charged premium rates *more than* adequate to cover the long-term operating costs and losses of the programs even before any changes were made to implement the DSB's recommendations and rulings, the changes can only result in even more favorable financial results.

7. Brazil's emphasis on the original subsidy estimates for the 2006 and 2007 cohorts in the U.S. budget data – and the alleged "guaranteed loan subsidy" for the GSM 102 program – cannot be credited. The original "subsidy" estimate is made well before virtually any activity in the program has occurred in the fiscal year and begins with a historically overly-optimistic projection of actual use of the program. The requirement to use government-wide estimation rules – including mandated risk assessment country grades – without regard to the actual experience specific to the CCC export credit guarantee programs routinely results in initial overestimation of both utilization of the programs and a corresponding overestimation of guaranteed loan subsidy estimates.

8. There is also no textual basis for Brazil's suggestion that an appropriate method of assessing "benefit" under Article 1.1(b) of the *SCM Agreement* is simply to compare fees of different guarantees, and it ignores the myriad reasons why fees might be different for different guarantees. A difference in fees does not necessarily reflect that any "benefit" is being conferred. Brazil's comparison of GSM 102 fees to Ex-Im Bank fees is flawed, all the more so given that Brazil has not even taken into account *other* guarantees available in the marketplace.

9. **– The United States has not provided export credit guarantees under the GSM 102 program inconsistently with Articles 10.1 and 8 of the *Agreement on Agriculture*.** Article 10.1 of the *Agreement on Agriculture* prohibits the provision of export subsidies (other than those listed in Article 9.1) "in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments." While Article 1(e) of the *Agreement on Agriculture* defines "export subsidies" as "subsidies contingent upon export performance," there is no further elaboration as to the kinds of measures that meet this definition. Accordingly, the panel in the original proceeding found that the *SCM Agreement* – which also includes provisions dealing with export subsidies – could provide useful "contextual guidance." The fact that the GSM 102 export credit guarantees are not export subsidies within the meaning of item (j) is relevant to the question under the *Agreement on*

Agriculture, and supports a finding that GSM 102 guarantees are not export subsidies for purposes of Articles 8 and 10.1 of that Agreement.

10. **– The United States has "taken action" to withdraw the subsidy with respect to GSM 102, GSM 103, and SCGP export credit guarantees issued prior to 1 July 2005.** There are no export credit guarantees "still outstanding" under the SCGP program. To the extent there are any export credit guarantees outstanding under the GSM 102 and GSM 103 programs, the United States has "taken action" with respect to them by changing the cost and fee structure of the entire portfolio of programs of which they are part. The United States ceased to provide "export credit guarantee . . . programs at premium rates which are inadequate to cover the long-term operating costs and losses of the programs" and, thus, withdrew the subsidy with respect to these export credit guarantees regardless of when they were issued.

11. **Actionable Subsidies – Brazil fails to substantiate its arguments that the effects of eliminating the Step 2 program are "relatively modest."** Brazil fails to substantiate its claims that the elimination of the Step 2 program is insufficient to meet the U.S. obligation "to remove the adverse effects [of]" the subsidy found to cause serious prejudice in the original proceeding. Brazil's primary argument is that the counter-cyclical payment rate will increase due to a drop in U.S. farm prices following elimination of the Step 2 program. However, Brazil cannot show that this will happen in the current marketing year (*i.e.*, in the year that is relevant for Brazil's "present" serious prejudice claims). To the contrary, the season average farm price is projected to be below the marketing loan threshold of 52 cents/lb in the current marketing year (and would likely have been below the threshold even if the Step 2 program were in effect). In these circumstances, the marketing loan rate – and not the season average farm price – is factored into the calculation of the counter-cyclical payment rate and no drop in the season average farm price (whether due to elimination of the Step 2 program or any other reason) will result in any change in the counter-cyclical payment rate. Moreover, even in future years, any possible increase is likely to be small and less than the price effect of the elimination of the Step 2 program.

12. Brazil also fails to explain that elimination of the Step 2 program likely has caused *lower* marketing loan program payments because of a resulting increase in world prices and, thus, also in the adjusted world price (or "AWP") that is calculated on the basis thereof. Since marketing loan payments are calculated as the difference between the AWP and the 52 cents/lb marketing loan threshold, an increase in the AWP results in a concurrent *decrease* in payments under the marketing loan program. Thus, elimination of the Step 2 program is likely to *minimize* any adverse effects that Brazil claims are being caused by the marketing loan program. Any positive effect of reducing the amount of marketing loan payments, in turn, further amplifies the impact on the market of eliminating the Step 2 program.

13. In addition, Brazil argues that the effect of eliminating the Step 2 program is allegedly "relatively modest" because the program is smaller in size than the counter-cyclical payment program and marketing loan program. However, Brazil has acknowledged before that the focus of the serious prejudice analysis is on the effect of the challenged subsidy, not its size (and that size does not necessarily say anything about effect). Indeed, in the original proceeding, Brazil considered that the Step 2 program had the second largest impact on world prices and exports, even though payments were smaller under that program than others. Brazil also ignores its own earlier arguments that the "production effects" of the Step 2 program are only one way in which, in Brazil's view, Step 2 payments could have affected world market prices. Brazil fails to take into account the other effects it alleged in the original proceeding, including the alleged "export-enhancing" nature of the program. Moreover, to the extent that it is even possible to draw conclusions from the data available for the first three months of MY 2006, the data do not appear to support Brazil's conclusion that elimination of the Step 2 program has had "relatively modest" effects on production, exports, and world prices.

14. **Brazil does not demonstrate that the marketing loan or counter-cyclical payment program mandate a breach of U.S. obligations under Articles 5(c) and 6 of the *SCM Agreement*.** Brazil appears to be challenging, as such, the U.S. marketing loan and counter-cyclical payment *programs*, which the United States understands to be the legal/regulatory provisions for the grant or maintenance of the subsidies. As Brazil has recognized both in this dispute and others, it is established under WTO law that a Member can only challenge measures of another Member *per se* (i.e., "as such") if such measures mandate a violation of the WTO Agreement. Brazil has not shown that the legal/regulatory provisions for the grant or maintenance of marketing loan and counter-cyclical payments mandate a breach of Articles 5(c) and 6.3(c) or 6.3(d) of the *SCM Agreement*.

15. **Brazil fails to make a *prima facie* case of WTO-inconsistency under Articles 5(c) and 6.3(c) of the *SCM Agreement.*** Brazil fails to make a *prima facie* case that "the effect" of the marketing loan and counter-cyclical payment programs is "significant price suppression" within the meaning of Article 6.3(c) of the *SCM Agreement*. That is, therefore, not a basis for a finding of serious prejudice within the meaning of Article 5(c) of the *SCM Agreement*.

16. **– Evidence regarding the structure, design, and operation of the counter-cyclical and marketing loan payment programs do not support Brazil's claims.** Although Brazil asserts that "the nature" of the counter-cyclical payment program, in terms of its structure, design and operation, provides evidence of a causal link between the program and the alleged present "significant price suppression," Brazil fails to take into account the recent empirical research finding that there is no evidence that counter-cyclical payments are the cause of any significant changes in plantings. This empirical research was not available at the time the original panel reviewed the counter-cyclical payment program.

17. There also continues to be substantial evidence showing that decoupled payments, such as counter-cyclical payments, are capitalized into land values and land rents. Where land is rented – and the data show that a substantial portion (almost half) of all U.S. farmland was rented in 2005 – some amount of the value of decoupled payments is transferred from operators (to whom the payments are actually made) to the owners of base acres in the form of higher rents and sales values, thereby minimizing further any possible effects that counter-cyclical payments may have on production.

18. The empirical research regarding the minimal production effects of the counter-cyclical payment program is bolstered by data that show that traditional U.S. cotton farms receiving cotton counter-cyclical payments planted *approximately 40 percent fewer cotton acres* over MY 2002-2005 than they had in the period used to calculate cotton base acres. This decline in cotton planted acres on traditional U.S. cotton farms reflects the fact that other factors, such as weather and competing crops drive planting, not counter-cyclical payments.

19. In the case of marketing loan payments, Brazil has acknowledged (through its economist) that whether marketing loan payments have any effect on production depends on, *inter alia*, producers' *expectations at the time of planting* both as to prices for the harvested crop and of payments. Despite this, to support its arguments about the effects of the marketing loan program, Brazil points to data showing that the *actual* AWP rates in MY 1999-present have been below the loan rate in a number of years. Since farmers did not know at the time of planting what the *actual* AWP would be during the marketing year commencing up to seven months later, however, a comparison of the *actual* AWP to the loan rate says nothing about whether the marketing loan program actually affected farmers' planting decisions from MY 1999 to the present. An examination of the planting decisions made by U.S. producers in the light of the actual conditions as they existed as of the time of planting shows that in many of the marketing years since MY 1999 – including the present marketing year (MY 2006) – *expected prices were higher than the loan rate*. Under these conditions, it cannot be said that the marketing loan distorted U.S. producers' production decisions. Even in other years, however – in which marketing loan payments could possibly have had an effect on planting –

information about actual planting decisions show that they were, in fact, shaped by market factors, not the expectation of marketing loan payments.

20. Brazil's emphasis on what it terms variously the "large," "very large," "huge," and "massive" government outlays under the marketing loan and counter-cyclical payments programs is misplaced. The size of government outlays alone says nothing about their effect, if any, on world market prices. Moreover, Brazil's allegations of the "advantage" given by the counter-cyclical payment and marketing loan payment programs to U.S. producers and exporters to lower their prices and increase their market share are unsubstantiated and do not support Brazil's claim of significant price suppression.

21. **– The facts demonstrate that U.S. producers and exporters have reacted to market signals and are not "insulated" by the marketing loan and counter-cyclical payment programs.** The facts do not support Brazil's argument that the marketing loans and counter-cyclical payment programs "fuel" plantings and production by "insulating" U.S. producers and exporters from normal market signals. To the contrary, U.S. share of world production has been *stable* over the life of the FSRI Act. This reflects the fact that U.S. production has increased and decreased in much the same way as production elsewhere in the world. Similarly, U.S. share of world *exports* has been stable over the life of the Farm Security and Rural Investment Act of 2002 ("the FSRI Act"). Even the increase in U.S. share of world market exports that occurred between MY 1999 and MY 2002 is the result of market conditions (primarily, the decline in U.S. mill use and corresponding increase in consumption elsewhere), not "the effect" of the counter-cyclical payment and marketing loan payment programs. Thus, neither U.S. production nor U.S. export behavior supports the claim that U.S. producers and exporters are insulated from market forces as Brazil alleges.

22. Contrary to Brazil's assertions, Brazil does not demonstrate a "strong link" between the counter-cyclical payment and marketing loan payment programs, on the one hand, and world market prices, on the other, through its attempts to show the *absence* of a "link" between "prices" and U.S. planted acreage, production, and exports. Brazil's argument about the absence of such a link seems to be inconsistent with its arguments elsewhere that the U.S. market is the "single most important market" in *influencing* cotton prices. Moreover, Brazil's analysis of the sensitivity of U.S. planted acreage, production, and exports to prices is flawed.

23. <u>First</u>, Brazil's comparison of planted acreage to New York futures prices for cotton *alone* ignores the fact that the cotton futures prices is *not* the sole basis for a farmer's planting decision; other factors including, *inter alia*, the futures prices of competing crops are important considerations. <u>Second</u>, Brazil's comparison of U.S. upland cotton production to actual prices again assumes, incorrectly, that planting decisions could be explained through an examination of cotton prices alone. It also assumes incorrectly that U.S. farmers *know* at the time that they plant (in January-March of a given year) what the actual farm price will be in the upcoming marketing year, which does not even start until August. <u>Third</u>, Brazil's comparison of upland cotton exports and farm price fails to take into account the market conditions – for example, important developments in the U.S. textile and apparel industry – that were responsible for the changes in U.S. export patterns in the period MY 1998 to 2002. It also fails to address the fact that *since the FSRI Act came into effect*, U.S. share of world exports has been fairly stable, showing that U.S. exporters have reacted to market conditions in the same general way as foreign exporters.

24. – "Absolute" increases in U.S. production are "the effect" of improvements in yields, not the marketing loan and counter-cyclical payment programs. Brazil argues erroneously that an increasing "*absolute*" volumes of U.S. production of upland cotton from MY 2002-2005 are indicative of alleged trade-distortive effects of the U.S. marketing loan and counter-cyclical payment program. The increasing *absolute* volumes of production were the result of *record U.S. yields* in the period from MY 2002 though 2004, not the counter-cyclical payment and marketing loan payment programs.

There is no basis for Brazil's argument that any increase due to yield improvements should nonetheless be attributed to the counter-cyclical payment and marketing loan payment programs.

25. **– Brazil fails to demonstrate a "temporal coincidence" between marketing loan payments and counter-cyclical payments and the alleged price suppression.** Contrary to Brazil's assertions, it does not identify facts that "reinforce" the original panel's finding of a discernable temporal coincidence between U.S. subsidies and price suppression. Instead, consideration of each of the factors reviewed by the original panel in coming to this conclusion demonstrate that there is no such temporal coincidence now. First, U.S. planted acreage has been stable for the entire period that the FSRI Act has been in effect and is lower now than in the period examined in the original proceeding; there has been no "overall increase" in plantings similar to that observed by the panel in the original proceeding. Second, U.S. share of production has *not* increased over the period of the FSRI Act, as it appeared to do between MY 1998 and MY 2002, the period examined by the original panel. Third, the U.S. prices received by U.S. upland cotton producers have not decreased since the FSRI Act came into effect. Fourth, while the A-Index in MY 2002-2005 was lower than the 1980-2001 average, this is not evidence of price *suppression*. Moreover, the fact that the A-Index has trended downwards for more than 25 years – from well before the FSRI Act came into effect – and that the A-Index has gone *up* from the levels that prevailed *before* the FSRI Act came into effect would tend to suggest that, to the extent there is any price *suppression*, it is not "the effect" of the marketing loan and counter-cyclical payment programs. Fifth, while the absolute volume of U.S. exports went up over the period of the FSRI Act, U.S. share of world exports did *not* increase. This shows that U.S. export behavior is shaped by the same market forces that shape the behavior of foreign producers and exporters, not by "U.S. subsidies." Sixth, there have been low levels of U.S. cotton imports for decades; this has little to do with the programs under the 2002 FSRI Act. In short, none of these factors support a finding of a "temporal coincidence" now with respect to the marketing loan and counter-cyclical payment programs.

26. **– Brazil does not demonstrate that U.S. producers would "switch to alternative crops" in the absence of payments under the marketing loan and counter-cyclical payment programs.** Brazil fails to show that "but for" the marketing loan and counter-cyclical payment programs, many upland cotton producers would have had to discontinue growing upland cotton and switch to alternative crops. Brazil's argument is based on the incorrect assumption that decisions about whether to plant cotton or an alternative crop are made by reference to the "long-term total costs of production" of upland cotton. That assumption is inconsistent with the accepted principle in agricultural economics that the measure producers use when deciding what crops to grow is *variable costs* of production, not "long-term total costs of production." The data show that, in the period MY 2002 to 2005, U.S. producers have not only covered variable costs but in almost all years have covered most if not all of their total costs of growing cotton as well.

27. Total costs may be relevant, for example, to such long-term decisions as whether to continue or exit cotton farming. However, those decisions are not made on the basis of a segmented cotton-only analysis of costs and returns that Brazil presents in its first written submission. Rather, those types of whole-farm decisions will be made taking into consideration whole-farm costs and returns, including, for example, costs and revenue generated from other crops that have been (or may be) grown as well as off-farm revenues. Brazil has provided no analysis of whole farm costs and revenues that would support its conclusion that, absent payments under the marketing loan and counter-cyclical payment programs, certain cotton producers in the United States would exit cotton farming altogether.

28. Brazil's analysis also ignores entirely the substantial number of producers who do not receive payments. Moreover, Brazil does not address the possibility that any exit of high-cost U.S. producers would be offset by the expansion of the production of more efficient lower-cost U.S. producers, leaving U.S. plantings and production at the same levels overall.

29. **– Brazil attempts to attribute the price effects of other factors to the marketing loan and counter-cyclical payment programs.** Brazil's claim that the U.S. marketing loan and counter-cyclical payment programs are "fueling" U.S. planting, production, and exports and thereby significantly suppressing world market prices is also premised on an overly-simplistic view of the world cotton market. Brazil ignores – and, in fact, attempts to attribute to the marketing loan and counter-cyclical payment programs – the effects of other factors, including, importantly, China's trade in cotton. While Brazil fails to provide evidence that the United States "drives" world market prices for upland cotton, there is substantial evidence of a close correlation between China's net trade in cotton and the A-Index. Thus, contrary to Brazil's assertions, the United States is not the most important market influencing cotton prices throughout the world, nor the "driver" of the world market price. Brazil's attempts to ascribe price-suppressive effects to the marketing loan and counter-cyclical payment programs on the basis of these representations – without properly addressing and distinguishing the effects of such other factors as the impact of China's net trade and trade policies – are untenable.

30. Indeed, what Brazil believes is the measure of the "world price" itself – the A-Index – has been changed to reflect the importance of China in the world cotton market. The A-Index is now no longer calculated on the basis of prices of cotton delivered to Northern Europe. Rather, the A-Index is now calculated on the basis of cotton delivered *to Far East ports*. This is not a mere "technical change," as Brazil alleges. The fact that such a shift was necessary to allow proper measurement of "international cotton price movements" and that this shift was driven primarily by the impact on the market of a single country – China – confirms what the market reports overwhelmingly recognize: the price trends for upland cotton cannot be explained except by accounting for China's influence on the market.

31. Moreover, contrary to Brazil's assertions, downward pressure on prices results from uncertainty about the reliability of China's supply and demand statistics as well as ***ad hoc*** **changes in government policies. Uncertainty leads to increased price volatility and risk to world market participants. These** effects are reflected in prices. This is even confirmed by the market reports that Brazil itself submits.

32. **– The econometric modeling cited by Brazil is flawed and greatly exaggerates any effects of removing the programs.** Even based on a preliminary review of the econometric model submitted by Brazil, it is apparent that the model relies on a series of flawed economic assumptions that grossly overstate any possible effect of removing the marketing loan and counter-cyclical payment programs. Contrary to Brazil's assertions, the important parameters used in the model are not commonly used by U.S. Department of Agriculture ("USDA") or Food and Agricultural Policy Research Institute ("FAPRI") economists. Indeed, the parameters in Brazil's new model are even more exaggerated than the parameters used in what Brazil termed was the "FAPRI-like" model presented in the original proceeding. Brazil now ascribes to the marketing loan and counter-cyclical payment programs almost the *same* price effects that it had previously ascribed to *six* programs (the marketing loan and counter-cyclical payment programs plus four others). The marketing loan and counter-cyclical payment programs have not changed; what has changed are the assumptions that Brazil makes to produce the more egregious effects.

33. The United States demonstrates that, when certain "key elasticities" and some other basic assumptions are re-calibrated to *actually* reflect FAPRI and other well-established parameters, the price effects predicted by Brazil's new model decline sharply (ranging, for example, from only 0.96 percent to 1.52 percent over the period MY 2006-2008). More detailed analysis and re-calibration would presumably reduce the price effects even more. Both this model and the World Bank study to which Brazil also cites greatly exaggerate any possible impact of removing the marketing loan and counter-cyclical payment programs. They are, thus, also inconsistent with other recent studies showing only minimal price impacts from removing those programs.

34. **– Brazil has not demonstrated that "the effect" of the marketing loan and counter-cyclical payment program is "significant" price suppression.** The *SCM Agreement* does not define "significant" price suppression. The ordinary meaning of significant, however, is "important, notable; consequential," which suggests that any price suppression must reach a level at which it is important, notable, and consequential in order to be inconsistent with Article 6.3(c). Brazil does little more than cite back to the same arguments it makes in its causation discussion to attempt to show "significant" price suppression. In so doing, Brazil effectively writes "significant" out of Article 6.3(c) altogether. Brazil does not explain how any of the arguments it makes in its causation discussion demonstrate that the *degree* of the alleged price suppression is "important, notable; consequential."

35. – **Brazil fails to make a *prima facie* case of WTO-inconsistency under Articles 5(c) and 6.3(d) of the *SCM Agreement.*** Brazil fails to make a *prima facie* case that the United States is causing "serious prejudice" to Brazil's interests within the meaning of Articles 5(c) of the *SCM Agreement* because "the effect" of U.S. marketing loan and counter-cyclical payment programs under the FSRI Act is an increase in the U.S. world market share within the meaning of Article 6.3(d) of the *SCM Agreement*. Even leaving aside the lack of legal basis for Brazil's claims against the programs, as such, Brazil does not demonstrate that all of the elements of Article 5(c) and 6.3(d) are satisfied.

36. In the original proceeding, the panel interpreted "world market share" under Article 6.3(d) to mean "share of the world market supplied by the subsidizing Member of the product concerned." Brazil has proposed two different measures of "supply" – either production in a marketing year or production plus beginning stocks in a marketing year. It is not necessary for the Panel to decide, for purposes of this proceeding, which is the more appropriate measure because *Brazil's claim fails under either approach*. First, while Brazil asserts its claim in respect of MY 2005, Brazil fails to segregate from the adverse effects it alleges any effects of the Step 2 program. Second, Brazil fails to demonstrate that the slight increase in share of world production or production plus beginning stocks over the average share in MY 2002-2004 "follows a consistent trend over a period when subsidies have been granted." To the contrary, the data show clearly that it is a part of the ordinary fluctuations in U.S. share of world production. This is true no matter how far back in time one looks. There is, therefore, no basis for Brazil's claim under Articles 5(c) and 6.3(d) of the *SCM Agreement*.

37. **Requests For Preliminary Rulings – Brazil's claims relating to GSM 102 guarantees in respect of exports of pig meat and poultry meat are outside the scope of this proceeding.** GSM 102 guarantees in respect of exports of pig meat and poultry meat have never been found to be WTO-inconsistent nor been subject to any DSB recommendation. Under these circumstances, the GSM 102 guarantees in respect of exports of pig meat and poultry meat are not measures taken to comply with the recommendations and rulings of the DSB and are not measures within the scope of this proceeding. Further, Brazil's claims under Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement* are outside the scope of this proceeding to the extent that they relate to GSM 102 guarantees in respect of exports of pig meat and poultry meat. There is no merit to Brazil's argument that it is entitled to re-assert its claims in respect of these GSM 102 guarantees because it "successfully appealed" the panel's findings regarding the GSM 102 guarantees in respect of exports of pig meat and poultry meat. Even though the original panel's findings were reversed, that changes nothing about the fact that the Appellate Body did not complete the legal analysis and, thus, made no finding of WTO-inconsistency against the measures (and the DSB also issued no rulings and recommendations addressed to them).

38. – **Brazil's claims in respect of the marketing loan and counter-cyclical payment programs are outside the scope of this proceeding.** To the extent that Brazil's claims of serious prejudice and threat of serious prejudice are against the marketing loan and counter-cyclical payment *programs* under the FSRI Act, the claims are outside the scope of this proceeding. The original panel made only one actionable subsidy finding – with respect to Brazil's claim of "present" serious

prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement* against certain *payments* made in MY 1999-2002. The marketing loan and counter-cyclical payment *programs* were not subject either to a finding of WTO-inconsistency or any DSB rulings and recommendations. They are, therefore, not measures within the scope of this proceeding. Moreover, Brazil's claims relating to these programs under Articles 5 and 6 of the *SCM Agreement* are not within the scope of this proceeding.

39. **– Brazil's claims against the marketing loan program and the counter-cyclical program are outside the scope of this dispute because these measures were not "taken to comply" under DSU Article 21.5.** Brazil's claims against the marketing loan and counter-cyclical payment programs are also outside the scope of these proceedings because the programs have not been changed in response to DSB recommendations and rulings or otherwise. Brazil may not renew in an Article 21.5 proceeding claims made in the original proceeding against a measure which is the same measure as in the original proceeding. In the present case, Brazil may not raise again the claims of serious prejudice or threat of serious prejudice under Article 5(c) and 6.3(c) and (d) of the *SCM Agreement* against the marketing loan payment program and the counter-cyclical program. These claims are outside the scope of this Article 21.5 proceeding.

40. – **Brazil's claims that there were no measures taken to comply in a past period are not within the scope of the proceeding.** Brazil claims that the United States failed to take measures to comply with the DSB's actionable subsidy-related recommendation in a timely fashion and seeks a finding that there was a period in the past (21 September 2005 to 31 July 2006) in which no measure taken to comply existed. However, as Brazil does not dispute that measures taken to comply exist, there is no "disagreement" (as required by Article 21.5) over the "existence" of measures taken to comply. There is also no textual basis for an exercise such as the one Brazil is seeking and it would seem contrary to the statement in DSU Article 3.7 that "the aim of the dispute settlement mechanism is to secure a positive solution to a dispute." Thus, Brazil's claim that there were no U.S. measures taken to comply between 22 September 2005 and 31 July 2006 is not within the scope of this proceeding.

ANNEX A-3

THIRD PARTY SUBMISSION OF ARGENTINA

(5 January 2007)

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I. INTRODUCTION

1. Argentina is grateful for this opportunity to give its views as a third party in this dispute. It will be making a series of comments on some of the arguments put forward by Brazil and the United States in their respective written submissions of 7 November and 15 December, without prejudice to any further comments at the meeting of the Panel with the parties and third parties.

2. Argentina will be referring to the following matters in particular:

(a) Deficiency of the measures taken by the United States to implement the DSB's recommendations and rulings regarding the actionable subsidies found to be inconsistent with the WTO Agreements.

(b) Inadequacy of the measures taken by the United States to implement the DSB's recommendations and rulings regarding the prohibited subsidies found to be inconsistent with the WTO Agreements.

II. ARGUMENTS

A. DEFICIENCY OF THE UNITED STATES' MEASURES REGARDING ACTIONABLE SUBSIDIES

3. Argentina agrees with Brazil that the United States has not fulfilled its obligation under Article 7.8 of the SCM Agreement in respect of the price-contingent subsidy programmes for upland cotton implemented under the Farm Security and Rural Investment (FSRI) Act of 2002, since the programmes have been neither withdrawn nor significantly changed.

4. Argentina agrees with Brazil that the measures taken by the United States are deficient in that, although the user marketing (Step 2) payments programme has been repealed, the marketing loan and counter-cyclical payments programmes remain intact.

5. In this regard, a recent document of the Congressional Research Service is enlightening in its statement that "... additional permanent modifications to US farm programs may still be needed to fully comply with the 'actionable subsidies' portion of the WTO ruling."[1]

6. Brazil produced conclusive evidence that the marketing loans and counter-cyclical programmes continue to have adverse effects on the interests of Brazil and other cotton-producing countries, such as Argentina, in the form of serious prejudice caused by significant price suppression.

7. Furthermore, following Brazil's assertion that withdrawal of the Step 2 programme could result in higher payments under the marketing loan and counter-cyclical programmes, in July 2005 Keith Collins, Chief Economist of the USDA, suggested that "... ending the Step 2 program would result in slightly lower domestic prices – by two to three cents per pound – and higher export prices for US cotton. […] that declines in producer prices would be likely to trigger an increase in counter-cyclical payments (CCP) to US cotton farmers that would offset losses from lower prices".[2]

8. Consequently, Argentina is of the view that the United States is not implementing the DSB's recommendation regarding the measures identified as actionable subsidies.

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[1] Congressional Research Service, RS22552, December 11, 2006, "Agricultural Issues in the 110th Congress", Ralph M. Chite, Specialist in Agricultural Policy Resources, Science, and Industry Division.

[2] Congressional Research Service, RS22187, September 8, 2006, "U.S. Agricultural Policy Response to WTO Cotton Decision". Randy Schnepf Specialist in Agricultural Policy Resources, Science, and Industry Division.

B. INADEQUACY OF THE UNITED STATES' MEASURES REGARDING PROHIBITED SUBSIDIES

9. In its written submission[3], the United States asserts that export credit guarantees have been provided under the GSM-102 programme subsequent to 1 July 2005, *consistently* with the United States' WTO obligations.

10. Argentina demurs: as Brazil held[4], the United States' "measures taken to comply" fail to implement adequately the recommendations and rulings of the DSB.

11. Argentina would point out that the original Panel found (and its finding was later confirmed by the Appellate Body) that the export credit guarantee programmes maintained by the US Commodity Credit Corporation (CCC) – the General Sales Manager 102 (GSM-102), General Sales Manager and the Supplier Credit-Guarantee (SCGP) programmes (GSM-103) – pertaining to exports of upland cotton and other agricultural products not included in the Schedule of Commitments supported under the programmes and one scheduled commodity (rice), are export subsidies applied in a manner which results in circumvention of the United States' export subsidy commitments within the meaning of Article 10.1 of the Agreement on Agriculture, and are therefore inconsistent with Article 8 of that Agreement. The Panel further found that such programmes constitute *per se* export subsidies prohibited by Article 3.1(a) and 3.2 of the SCM Agreement.

12. On the strength of those findings the DSB recommended that the United States *withdraw* the prohibited subsidies *without delay* in accordance with Article 4.7 of the SCM Agreement, and by 1 July 2005 at the latest.

13. Argentina's first observation is that although the United States was under an obligation to withdraw them "without delay" the programmes were still intact at 1 July 2005. Furthermore, the GSM-102, GSM-103 and SCGP programmes have still not been withdrawn in the strict sense of the term.

14. It is Argentina's understanding that, properly construed, the rule in question requires the United States not only to "withdraw" the prohibited subsidies but also to take steps to that end "without delay"; so for the obligation here, fulfilment is subject to a time factor. Argentina therefore believes that the time taken to implement "withdrawal" of the measure cannot be overlooked in assessing compliance with the above-mentioned requirements.

15. Secondly, Argentina points out that despite the DSB's recommendations and the provisions of Article 4.7 of the SCM Agreement, as concerns the GSM-103 and SCGP programmes the United States merely announced that no more applications would be accepted under the programmes as from 1 July 2005 and 1 October 2005 respectively. In Argentina's view, to stop there would be a lowering of standards in terms of the obligation laid down in Article 4.7 of the SCM Agreement which expressly prescribes "withdrawal" of the measure and not merely "non-acceptance of new applications", which appears to be the United States' interpretation judging from its assumption that by not accepting new applications it would be complying with the above-mentioned rule and with the DSB's recommendations.[5]

16. In Argentina's view, the negative consequences of allowing that assumption need to be stressed, since the prohibited subsidy still exists and so too, therefore, does its inconsistency with WTO rules.

[3] First Written Submission of the United States, point V.A. (page 30).
[4] First Written Submission of Brazil, point 10 (page 130).
[5] First Written Submission of the United States, pages 2, 8 and 66.

17. The Appellate Body's observation in *Brazil – Aircraft* (Article 21.5 – Canada) is enlightening in this regard:

> "Turning to the ordinary meaning of 'withdrawal', we observe first that this word has been defined as 'remove' or 'take away', and as 'to take away what has been enjoyed; to take from'. This definition suggests that 'withdrawal' of a subsidy, under Article 4.7 of the *SCM Agreement*, refers to the 'removal' or the 'taking away' of that subsidy. ... In our view, to continue to make payments under an export subsidy measure found to be prohibited is not consistent with the obligation to 'withdraw' prohibited export subsidies, in the sense of 'removing' or 'taking away'".[6]

18. In Argentina's view, it needs to be made clear that although in the dispute cited above payments continued to be made under an export subsidy measure found to be prohibited and in the present dispute the United States has announced that it will not continue to grant export credit guarantees, this does not exempt the United States from complying properly and without delay with the obligation laid down in Article 4.7 of the SCM Agreement.

19. In short, for Argentina, withdrawal of the measure as meant by the Panel in its recommendation implies <u>terminating the programme</u> and not merely suspending payments or refusing new applications.

20. Thirdly, Argentina agrees with Brazil that the changes introduced by the United States in the GSM-102 programme are insufficient to comply with the Panel's recommendation to *withdraw* the prohibited subsidies *without delay*, and are moreover *inconsistent* with Articles 10.1 and 8 of the Agreement on Agriculture and Article 3.1(a) and 3.2 of the SCM Agreement.

21. The GSM-102 programme constitutes a "financial contribution" "contingent upon export performance" which confers a "benefit" on the recipients, despite the changes in rates introduced by the United States, as Brazil shows in its written submission.[7] Consequently, the GSM-102 programme constitutes an export subsidy within the meaning of Articles 1 and 3.1(a) of the SCM Agreement, circumvention of the United States' reduction commitments under Article 10.1 of the Agreement on Agriculture in respect of upland cotton and other unscheduled agricultural products and in respect of certain products in the Schedule of Commitments (particularly rice), as well as a breach of Article 8 of the Agreement on Agriculture.

22. Furthermore, Argentina does not share the United States' interpretation in its assertion that GSM-102 export loan guarantees are not export subsidies under Articles 8 and 10.1 of the Agreement on Agriculture.[8]

23. Argentina accordingly considers that the United States is not complying with the DSB's recommendation to "withdraw without delay" the above-mentioned programmes identified as prohibited subsidies.

III. CONCLUSION

24. In the light of the foregoing, Argentina considers that the United States has not fully and properly complied with the DSB's recommendations, particularly: (a) the recommendations regarding the actionable subsidies, because the measures adopted are deficient; and (b) the recommendations regarding the prohibited subsidies, because the measures applied by the United States, are inadequate.

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[6] Report of the Appellate Body in *Brazil – Aircraft* (Article 21.5 – Canada), paragraph 45.
[7] First Written Submission of Brazil, point 10.3.2.2.1.
[8] First Written Submission of the United States, point V.A.2.

ANNEX A-4

THIRD PARTY SUBMISSION OF AUSTRALIA

(5 January 2007)

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TABLE OF CASES

Short Title	Full Case Title and Citation
Australia – Salmon (Article 21.5 - Canada)	Panel Report, *Australia – Measures Affecting Importation of Salmon – Recourse to Article 21.5 by Canada*, WT/DS18/RW, adopted 20 March 2000, DSR 2000:IV, 2031
Brazil – Aircraft (Article 21.5 – Canada I)	Appellate Body Report, *Brazil – Export Financing Programme for Aircraft –Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/AB/R, adopted 4 August 2000, DSR 2000:VIII, 4067
Brazil – Aircraft (Article 21.5 – Canada I)	Panel Report, *Brazil – Export Financing Programme for Aircraft – Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW, adopted 4 August 2000, as modified by the Appellate Body Report, WT/DS/46/AB/R, DSR 2000:IX, 4093
Canada – Aircraft (Article 21.5 - Brazil)	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/AB/RW, adopted 4 August 2000, DSR 2000:IX, 4299
Chile – Price Band System (Article 21.5 - Argentina)	Panel Report, *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products - Recourse to Article 21.5 of the DSU by Argentina*, WT/DS207/RW, 8 December 2006
EC – Bed Linen (Article 21.5 - India)	Appellate Body Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW, adopted 24 April 2003, DSR 2003:III, 965
Korea - Vessels	Panel Report, *Korea – Measures Affecting Trade in Commercial Vessels*, WT/DS273/R, adopted 11 April 2005
US – Softwood Lumber IV (Article 21.5 – Canada)	Appellate Body Report, *United States - Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada - Recourse by Canada to Article 21.5 of the DSU,* WT/DS257/AB/RW, adopted 20 December 2005
US – FSC	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations"* WT/DS108/AB/R, adopted on 20 March 2000, DSR 2000: III, 1619
US – FSC (Article 21.5 – EC II)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, 14 March 2006
US – Shrimp (Article 21.5 - Malaysia)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481
US – Upland Cotton	Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R, adopted 21 March 2005
US – Upland Cotton	Panel Report, *United States – Subsidies on Upland Cotton*, WT/DS267/R, and Corr.1, adopted 21 March 2005, modified by Appellate Body Report, WT/DS/267/AB/R

INTRODUCTION

1. Australia considers that these proceedings under Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU) raise a number of issues of systemic importance and legal interpretation, which Australia will address in this written submission. These issues are:

(a) The scope of Article 21.5 proceedings, in relation to the United States requests for preliminary rulings;

(b) the order of analysis concerning Articles 1.1 and 3.1(a) and item (j) of the Illustrative List of the *Agreement on Subsidies and Countervailing Measures (SCM Agreement)*, in relation to the prohibited subsidies claims, including whether an *a contrario* interpretation of item (j) is permissible; and

(c) in relation to the actionable subsidies claims, whether the United States, by repealing the Step 2 payment programme, but maintaining the two other price-contingent subsidies (payments under the marketing loan and counter-cyclical payment programmes), has taken appropriate steps to remove the adverse effects of the subsidies or to withdraw the subsidies, within the meaning of Article 7.8 of the *SCM Agreement* in accordance with the recommendations and rulings of the Dispute Settlement Body (DSB) with respect to those subsidies**.**

Australia reserves the right to raise other issues in the third-party hearing with the Panel.

A. SCOPE OF ARTICLE 21.5 PROCEEDINGS – REQUESTS FOR PRELIMINARY RULINGS

2. The United States, in its First Written Submission, requests a number of preliminary rulings that raise important systemic issues concerning the scope of Article 21.5 proceedings and require careful consideration of relevant jurisprudence of the Appellate Body and Article 21.5 Panels.

3. Australia recalls that Article 21.1 expressly provides that "prompt compliance with recommendations or rulings of the DSB is essential in order to ensure effective resolution of disputes to the benefit of all Members." Thus, one of the objectives of Article 21.5 is to "avoid a complaining Member having to initiate dispute settlement proceedings afresh when an original measure found to be inconsistent has not been brought into conformity with the recommendations and rulings of the DSB."[1] Australia submits that were the United States requests for preliminary rulings to be granted, Brazil would be forced to initiate dispute settlement proceedings afresh in respect of claims which properly would fall within the scope of these Article 21.5 proceedings.

4. Australia recalls that the scope of proceedings under Article 21.5 is to determine "the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings" of the DSB. The use of the disjunctive 'or' makes clear that Article 21.5 proceedings can address two different situations. The first is the 'existence' of measures taken to comply with DSB recommendations and rulings. Accordingly, a panel may consider a claim that a Member has not taken measures to comply. The second is the 'consistency' with a covered agreement of measures taken to comply with DSB recommendations and rulings. Accordingly, a panel may consider a claim that implementing measures taken by a Member are inconsistent with a covered agreement.[2]

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[1] *US - Softwood Lumber IV (Article 21.5 – Canada)*, para. 72.
[2] *See EC – Bed Linen (Article 21.5 - India)*, para. 79.

5. In considering the phrase 'measures taken to comply', the Appellate Body in *Canada – Aircraft (Article 21.5 – Brazil)* expressed the view that:

> … the claims, arguments and factual circumstances which are pertinent to the "measure taken to comply" will not, necessarily, be the same as those which were pertinent in the original dispute. Indeed, the utility of the review envisaged under Article 21.5 of the DSU would be seriously undermined if a panel were restricted to examining the new measure from the perspective of the claims, arguments and factual circumstances that related to the original measure, because an Article 21.5 panel would then be unable to examine fully the "consistency with a covered agreement of the measures taken to comply", as required by Article 21.5 of the DSU.[3]

6. Moreover, a Panel constituted under Article 21.5 of the DSU should consider the new measure "in its totality."[4] The fulfilment of this task requires that a panel consider both the measure itself and the measure's application provided that the specific claim has been made by the complainant when the matter is referred by the DSB for an Article 21.5 proceeding.[5]

7. The Appellate Body has identified situations where measures fall outside the scope of Article 21.5 proceedings. It has held that:

> [i]t would be incompatible with the function and purpose of the WTO dispute settlement system if a claim could be reasserted in Article 21.5 proceedings after the original panel or the Appellate Body has made a finding that the challenged aspect of the original measure is not inconsistent with WTO obligations, and that report has been adopted by the DSB.[6]

1. Request relating to GSM 102 programme in respect of pig meat and poultry meat

8. Taking this jurisprudence into account, Australia submits that Brazil's claims relating to General Sales Manager (GSM) 102 guarantees issued by the United States Commodity Credit Corporation in respect of exports of pig meat and poultry meat may properly be considered by the Panel.

9. Australia does not agree with the United States' submission that because there is neither a finding that GSM 102 guarantees in respect of pig meat and poultry meat are WTO-inconsistent nor that they are the subject of a DSB recommendation, that Brazil's claims concerning the application of the new measure in respect of pig meat and poultry meat fall outside the scope of Article 21.5 proceedings.[7]

10. The situation in the present case is not that of a measure that was not challenged in the original proceedings or, if challenged, was addressed in those proceedings and not found to be WTO-inconsistent.[8] The claim specifically made by Brazil in its request for establishment of this Panel relates to the WTO-consistency of a new measure – guarantees issued under the revised GSM 102

[3] *Canada – Aircraft (Article 21.5 – Brazil),* para. 41. *See also US - FSC (Article 21.5 – EC II),* para. 93.

[4] *US - Shrimp, (Article 21.5 - Malaysia),* para. 87.

[5] *Ibid.*

[6] *EC –Bed Linen (Article 21.5 - India),* para. 98.

[7] United States First Written Submission, paras. 27 and 28.

[8] Compare with *Chile – Price Band System (Article 21.5 – Argentina),* in which the Panel, at para. 7.141, set out the conditions under which an Article 21.5 panel may consider new claims which were not raised before the original panel.

programme – the revisions to which, as the United States acknowledges, were implemented in response to the rulings and recommendations of the DSB.[9] Brazil is entitled to request, and the Article 21.5 Panel is required to consider, the new measure in its totality, including the measure's application. Thus, while Brazil alleges that it is "entitled to re-assert" its claim concerning actual circumvention with respect to pig meat and poultry meat, in effect Brazil's claim relates to the WTO consistency of a new measure (the revised GSM 102 programme) implemented in response to the DSB rulings and recommendations which was not before the original panel.[10]

11. Australia therefore submits that the United States' request that the Panel reject Brazil's claims relating to GSM 102 guarantees in respect of exports of pig meat and poultry meat should be refused.

2. Request concerning Brazil's claims against the marketing loan and counter-cyclical payment programmes

12. The United States also seeks a preliminary ruling that Brazil's claims against the marketing loan and counter-cyclical payment (CCP) programmes fall outside the scope of the Article 21.5 proceedings on two grounds – that the two programmes were not subject to any finding of WTO-inconsistency or any DSB recommendations, and those programmes were not "measures taken to comply" within the meaning of Article 21.5.

13. The United States argues that the marketing loan and the counter-cyclical payment programmes are not measures to which the DSB recommendations and rulings were addressed since those recommendations and rulings concerned the programmes as applied and not as such, and therefore that Brazil's claims in relation to those programmes fall outside the scope of Article 21.5 proceedings.

14. Australia agrees that the Panel's findings of WTO inconsistency contained in paragraph 8.1(g)(i) of its Report related to the "mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA [marketing loan assistance] payments and CCP payments" rather than to the programmes *as such.*[11]

15. However, Australia does not agree with the United States that Brazil is seeking to challenge the marketing loan and counter-cyclical payment programmes *per se*. Australia is of the view that the focus of the case under Articles 5 and 6 of the *SCM Agreement* is the continuing effects of the unamended programmes (that is, payments made under the programmes) rather than the programmes *as such.* Australia submits that it is impossible to analyze the price-contingent subsidy measures (marketing loan programme payments and CCP payments) still in existence in isolation from the programmes that govern those measures. In so far as a consideration of those programmes is necessary to determine whether the continuing price-contingent subsidy measures cause significant price suppression causing serious prejudice to Brazil's interests, then Australia submits that such programmes may properly be considered by the Article 21.5 Panel.

16. Australia further submits that the fact that the marketing loan and counter-cyclical payments programmes have not changed does not prevent them from being considered by an Article 21.5 Panel in the context referred to above, when determining the existence or consistency of measures taken to

[9] United States First Written Submission, para. 72.

[10] Compare with *Canada – Aircraft (Article 21.5 - Brazil)*, paras. 36-37.

[11] In an exercise of judicial economy, the Panel did not address Brazil's *per se* claims relating to the measures [allegedly mandatory legislative provisions and implement regulations providing for the payment of Step 2 payments, marketing loan programme payments, direct payments, counter-cyclical payments and crop insurance payments] under Articles 5(c) and 6.3(c) and (d) of the *SCM Agreement* and Articles XVI:1 and XVI:3 of the *GATT 1994*: *US – Cotton*, para. 7.1511.

comply with the recommendations and rulings concerning payments made under those programmes (the measures at issue in the original proceedings).

17. Australia therefore submits that the United States' requests concerning the marketing loan and counter-cyclical payment programmes should be refused.

3. Request concerning Brazil's claims that there were no measures taken to comply between 21 September 2005 and 31 July 2006

18. The United States seeks a preliminary ruling to the effect that Brazil's claims that there were no measures taken to comply in a past period (21 September 2005 to 31 July 2006) are not within the scope of these Article 21.5 proceedings. The United States argues that "DSU Article 21.5 does not provide that the task of the Panel is to decide – or, rather, declare – whether measures were taken to comply 'in a timely fashion.' In fact, DSU Article 21.5 does not refer to the issue of "timeliness" of implementation at all."[12]

19. Australia notes that the role of an Article 21.5 Panel is to examine the existence or consistency of measures taken to comply, and submits that an examination of "existence" of measures taken to comply can encompass a finding that no measures taken to comply exist within the meaning of Article 21.5 of the DSU. Such a finding was made by the Panel in *Australia – Salmon (Article 21.5 – Canada)*. In that case, the Panel found that because the date of entry into force of measures taken to comply by Australia occurred subsequent to the date upon which the reasonable period of time for implementation expired, for the period of time that the new measures did not apply subsequent to that date, "no measures taken to comply existed … in the sense of Article 21.5."[13]

20. Australia submits that a preliminary ruling cannot be granted in a way that would void rights under Article 22 of the DSU. This is because Article 3.2 of the DSU makes clear that "recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements." Pursuant to Article 1.2 of the DSU, the rules and procedures of the DSU, including those contained in Article 22, apply to disputes brought under the covered agreements "subject to such special or additional rules and procedures on dispute settlement … as are identified in Appendix 2." Australia notes that both Articles 7.8 and 7.9 of the *SCM Agreement* are listed in Appendix 2 to the DSU as "special or additional rules and procedures" on dispute settlement contained in the covered agreements. These Articles do not preclude the application of Article 22 of the DSU. Indeed, Article 22 rights would logically ensue from findings of inconsistency with Articles 7.8 and 7.9 of the *SCM Agreement*,[14] which are findings that are entirely within the Panel's mandate to make.

21. Australia therefore submits that the Panel should refuse the request of the United States for preliminary rulings with respect to Brazil's claim concerning the United States' failure to take measures to comply within the period 21 September 2005 – 1 August 2006, as this could diminish Brazil's rights under Article 22 of the DSU.

[12] United States First Written Submission, para. 51.

[13] *Australia – Salmon (Article 21.5 - Canada)*, para. 7.30.

[14] Australia notes that this position is consistent with the actions of both Brazil and the United States with respect to Brazil's request for authorization to take countermeasures pursuant to Article 22.2 of the DSU and Article 7.9 of the SCM (WT/DS267/26) and the United States' request for arbitration under Article 22.6 of the DSU and Article 7.10 of the *SCM Agreement* (WT/DS267/27).

B. CLAIMS CONCERNING EXPORT CREDIT GUARANTEES (EXPORT SUBSIDIES)

22. Brazil alleges that despite changes introduced by the United States on 1 July 2005 to the General Sales Manager 102 (GSM 102) export credit guarantee programme, that programme and the guarantees issued thereunder continue to constitute export subsidies under Articles 1, 3.1(a) and 3.2 of the *SCM Agreement*, as well as under item (j) of the Illustrative List of Export Subsidies included as Annex 1 to the *SCM Agreement* ("Illustrative List"). Further, since 1 July 2005, Brazil alleges that the United States has applied those export subsidies in a manner that results in circumvention of the United States' export subsidy commitments for unscheduled products and three scheduled products – rice, pig meat and poultry meat, in violation of Articles 10.1 and 8 of the *Agreement on Agriculture*.[15] Brazil argues that the Panel should only consider its claim under item (j) in the Illustrative List in the alternative, if the Panel finds that GSM 102 export credit guarantees are not export subsidies under Articles 1.1 and 3.1(a) of the *SCM Agreement.* The United States argues that the analysis of the revised GSM 102 programme should proceed from item (j) of the Illustrative List.

23. Australia submits that as the complaining party, Brazil has the right to identify a measure as an export subsidy according to a particular definition (for example, pursuant to Articles 1.1 and 3.1(a) of the *SCM Agreement)* and then to argue under another definition "in the alternative". Australia therefore submits that the Panel should address the argument made by Brazil relating to item (j) "in the alternative" after the principal claim under Articles 1.1 and 3.1(a) of the *SCM Agreement*.[16]

24. Australia further submits that even if the United States' approach were to be adopted, a finding by the Panel that the GSM 102 programme, as amended, did not fall within the terms of item (j) of the Illustrative List would not necessarily be determinative of whether the GSM 102 programme otherwise constituted an export subsidy under the relevant provisions of the *SCM Agreement.* In other words, an *a contrario* interpretation of item (j) is not permissible[17], and the Panel would not be precluded by such a finding from examining the consistency of the revised GSM 102 with Articles 1.1 and 3.1(a) of the *SCM Agreement.*[18] As has been recognized in a number of proceedings, the Illustrative List is just that – it is a purely illustrative list and does not, as the United States acknowledges, purport to be an exhaustive list of export subsidies.[19]

C. CLAIMS CONCERNING ACTIONABLE SUBSIDIES

25. Australia submits that in relation to Brazil's actionable subsidies claims, the Panel should consider whether the United States, by repealing the Step 2 payment programme, but maintaining the two other price-contingent subsidies (payments under the marketing loan and counter-cyclical payment programmes), has taken appropriate steps to remove the adverse effects of the subsidies or to withdraw the subsidies, within the meaning of Article 7.8 of the *SCM Agreement* in accordance with the DSB's recommendations and rulings with respect to those subsidies**.**

[15] Brazil First Written Submission, paras. 348-350.

[16] In *US – FSC*, the Appellate Body at para. 89 found no legal error in the Panel adopting the order in which the European Communities as claimant had presented its arguments under Articles 1 and 3 of the *SCM Agreement*, and rejected the United States' assertion that the analysis should have proceeded from footnote 59 to item (e) of the Illustrative List.

[17] *Korea – Vessels*, para. 7.207. In that case, the Panel found that Korea had failed to demonstrate that item (j) was applicable as an affirmative defence for those measures that were found to be in violation of Article 3.1(a) of the *SCM* Agreement: *Ibid.* para. 7.202. In reaching its conclusions, the Panel adopted the approach taken by the Panel in *Brazil – Aircraft (Article 21.5 - Canada I)* at paras. 6.37 *ff.*

[18] In *Brazil – Aircraft (Article 21.5 – Canada I)*, the Panel acknowledged that it was legally possible that there existed prohibited export subsidies within the meaning of Article 3.1(a) that did not fall within the scope of Annex I: *see* para. 6.30.

[19] *Ibid.*

26. Australia recalls that the Panel found that:

> the effect of the mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA [marketing loan assistance] payments and CCP [counter-cyclical payment] payments – is significant price suppression in the same world market within the meaning of Articles 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement.*[20]

27. In the light of this conclusion, the Panel recalled that, pursuant to Article 7.8 of the *SCM Agreement* "upon adoption of this report, the United States is under an obligation to 'take appropriate steps to remove the adverse effects or … withdraw the subsidy'".[21]

28. Australia notes that the United States eliminated the Step 2 payments in response to the DSB's recommendations and rulings. The other two "mandatory price-contingent United States subsidy measures" that were the subject of the Panel's findings remain in existence. Australia therefore submits that in so far as these measures still exist, the Panel may properly consider whether the United States has fulfilled its obligations under Article 7.8 of the *SCM Agreement.*

29. Australia recalls that in making the findings referred to above, the original Panel examined each price-contingent subsidy measure in turn[22] and made a number of findings relating to the effect of each measure individually, before considering the collective operation of those measures. It is clear from the Panel's analysis that each of the price-contingent measures individually were found to have a trade-distorting effect.[23] With respect to the marketing loan programme payments, the Panel stated that:

> We have no doubt that the payments stimulate production and exports and result in lower world market prices than would prevail in their absence. Moreover, the text of the measure indicates that the payments are mandatory, where certain market conditions prevail.[24]

The Panel further found that:

> … the structure, design and operation of the marketing loan programme has enhanced production and trade-distorting effects. The payments stimulate production and exports and result in lower world market prices than would prevail in their absence.[25]

On counter-cyclical payments, the Panel concluded that:

> … CCPs may influence production decisions indirectly by reducing total and per unit revenue risk associated with price variability in some situations … We have confirmed a strong positive relationship between upland cotton (base acre) producers receiving annual payments and upland cotton production. Moreover, the payments are mandatory, under certain market conditions.[26]

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[20] *US – Cotton*, para. 8.1(g)(i); *see also* para. 7.1416.
[21] *Ibid.*, para. 8.3(d).
[22] *Ibid.*, para. 7.1290.
[23] *Ibid.*, paras. 7.1290–1303.
[24] *Ibid.*, para. 7.1291 (footnote omitted).
[25] *Ibid.*, para. 7.1295.
[26] *Ibid.*, para. 7.1302.

Australia submits that these findings remain relevant to the present proceedings.

30. Australia therefore submits that the present Panel should, as part of its consideration of whether the United States has complied with its obligations under Article 7.8, determine whether the continued existence of the two price-contingent subsidy measures that were the subject of the original Panel's finding cause significant price suppression constituting serious prejudice to the interests of Brazil.

31. In other words, the Panel should examine whether repeal of the Step 2 programme together with the continued existence of the other two price-contingent subsidy measures resulted in full compliance with the United States' obligation to remove the adverse effects or withdraw the subsidies found by the Panel to exist with respect to all three price-contingent subsidies. Australia submits that this is consistent with the approach that Brazil has taken in this dispute.

CONCLUSION

A. Scope of Article 21.5 proceedings - Requests for preliminary rulings

32. For the reasons set out in this submission, Australia requests that the Panel:

(a) refuse the United States' request that the Panel reject Brazil's claims relating to GSM 102 guarantees in respect of exports of pig meat and poultry meat;

(b) refuse the United States' requests for preliminary rulings concerning the marketing loan and counter-cyclical payment programmes; and

(c) refuse the request of the United States for preliminary rulings with respect to Brazil's claim concerning the United States' failure to take measures to comply within the period 21 September 2005 – 1 August 2006.

B. Claims concerning export credit guarantees (export subsidies)

33. For the reasons set out in this submission, Australia submits that the Panel should address the argument made by Brazil relating to item (j) "in the alternative" after the principal claim under Articles 1.1 and 3.1(a) of the *SCM Agreement*.

34. If, however, the Panel were to adopt the order of analysis proposed by the United States, a finding by the Panel that the GSM 102 programme, as amended, did not fall within the terms of item (j) of the Illustrative List would not preclude the Panel from examining the consistency of the revised GSM 102 with Articles 1.1 and 3.1(a) of the *SCM Agreement.*

C. Claims concerning actionable subsidies

35. For the reasons set out in this submission, Australia submits that in so far as the price-contingent subsidy measures still exist, the Panel may properly consider whether the United States has fulfilled its obligations under Article 7.8 of the *SCM Agreement*. As part of its consideration of whether the United States has complied with its obligations under Article 7.8, Australia further submits that the Panel should determine whether the continued existence of the two price-contingent subsidies that were the subject of the original Panel's finding cause significant price suppression constituting serious prejudice to the interests of Brazil.

ANNEX A-5

THIRD PARTY SUBMISSION OF CANADA

(5 January 2007)

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I. EXECUTIVE SUMMARY

1. Canada agrees with Brazil that the United States has failed to fully implement the recommendations and rulings of the Dispute Settlement Body (DSB), and that the United States continues to provide subsidies that cause and threaten to cause serious prejudice within the meaning of Articles 5 and 6 of the *Agreement on Subsidies and Countervailing Measures* (*SCM Agreement*) and Article XVI:1 of the *General Agreement on Tariffs and Trade 1994* (GATT 1994).

2. Canada makes submissions with respect to two issues: the U.S. contention that marketing loan and counter-cyclical payment programmes should not properly be the subject of this proceeding; and the standard for threat of serious prejudice under Article 5(c) and footnote 13 of the *SCM Agreement*, and Article XVI:1 of the GATT 1994.

3. On the first issue, the United States argues that as an Article 21.5 proceeding applies only to "measures taken to comply with the recommendations and rulings" of the DSB, the panel cannot consider unchanged measures. This fails to recognize that a panel in an Article 21.5 proceeding is required to consider the context, and not merely individual measures, when determining compliance. The Panel here cannot properly evaluate U.S. compliance without considering the effect of the U.S. failure to do anything about the marketing loan and counter-cyclical payment programmes.

4. On the question of "threat", Canada submits that the ordinary meaning of the term, read in the context of the *SCM Agreement* and considered in the light of that agreement's object and purpose, supports this finding. By contrast, there is nothing in the *SCM Agreement* to support the U.S. contention that "a clearly foreseen and imminent likelihood of future serious prejudice", such as that required in Article 15.7 of the *SCM Agreement*, is *required* for a finding of threat of serious prejudice under Article 5(c) and footnote 13. The notion of threat is a flexible one, sufficiently flexible to address programmes that give rise to a constant and high probability of support to U.S. farmers, which in turn constitutes a permanent threat of serious prejudice.

II. INTRODUCTION AND BACKGROUND

5. Canada appreciates the opportunity to participate in this proceeding under Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU), having participated in previous proceedings before the original panel and Appellate Body.[1]

A. FINDINGS OF THE PANEL AND APPELLATE BODY

6. On 3 March 2005, the Appellate Body upheld the original panel's finding, *inter alia*, that particular U.S. measures set out in the *Farm Security and Rural Investment Act of 2002* (*FSRI Act*) were subsidies causing adverse effects, contrary to Articles 5 and 6 of the *SCM Agreement*.

7. Specifically, the Appellate Body upheld the original panel's finding in respect of so-called "price-contingent subsidies".[2] These subsidies – marketing loan programme payments, user marketing (Step 2) payments, marketing loss assistance payments and counter-cyclical payments – were found to result in significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, and thus constitute serious prejudice within the meaning of Article 5(c).

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[1] *United States – Subsidies on Upland Cotton*, Report of the Panel, WT/DS267/R, adopted 21 March 2005 ["*United States – Upland Cotton*, Panel Report"] and *United States – Subsidies on Upland Cotton*, Report of the Appellate Body, WT/DS267/AB/R, adopted 21 March 2005 ["*United States – Upland Cotton*, Appellate Body Report"].

[2] *United States – Upland Cotton*, Appellate Body Report, at para. 763(c)(i).

B. MEASURES TAKEN BY THE UNITED STATES

8. The United States claims that it has complied with the recommendations and rulings of the DSB. On 8 February 2006, the United States announced the repeal, effective as of 1 August 2006, of the Step 2 payment programme for upland cotton, one of the programmes found to be causing serious prejudice. This is the only measure the United States has taken to comply with the recommendations and rulings respecting serious prejudice.[3] The United States argues that the original panel was considering the collective effect of these payments and not the programmes in themselves. As a result, the United States argues, Brazil's claim that U.S. measures taken to comply in some respects do not exist, and to the extent they do exist, are not consistent with the *Agreement on Agriculture* and the *SCM Agreement,* are without basis.[4]

III. ARGUMENT

9. Brazil argues that the U.S. counter-cyclical and marketing loan payment programmes have an ongoing, pernicious effect on the world cotton market, which arises in part from the threat that these programmes will provide seemingly-unlimited support to U.S. cotton producers. At issue is whether these programmes (under which payments made were found to be mandatory price-contingent subsidies causing significant price suppression, thus constituting serious prejudice)[5] threaten to cause serious prejudice simply by virtue of their existence.

10. The standard to be applied for a determination of threat of serious prejudice is not necessarily, as the United States has argued, a "clearly foreseen and imminent likelihood of future serious prejudice" akin to that in Article 15.7 of the *SCM Agreement*.[6] Canada submits that there is no single test for establishing the existence of a "threat". Rather, "threat" may be analyzed both as a temporal concept as in Article 15.7, *and* as a probability of occurrence. Certain subsidy programmes, by their very nature, give rise to a constant likelihood of support that results in a permanent threat of serious prejudice. This stems from the fact that when certain economic conditions exist – conditions that we know *will* re-occur simply by virtue of the vagaries of the market and fact that the United States itself may at its discretion set the threshold for payments – the subsidies will necessarily be distributed.

11. In this regard, there is no uncertainty. The marketing loan and counter-cyclical programmes create a constant likelihood of support for U.S. farmers, thus having the very real potential to distort international trade. These programmes were found by the original panel and the Appellate Body to be subsidies causing serious prejudice. And these programmes *must* pay to producers when certain conditions exist. If such programmes do not constitute a threat of serious prejudice, it is difficult to conceive of any subsidy that could have the potential to distort international trade and constitute a threat of serious prejudice to the interests of other Members.

[3] *Deficit Reduction Act of 2005*, U.S. Public Law 109-171, Section 1103, online: http://www.access.gpo.gov/nara/publaw/109publ.html. See also First Written Submission of the United States (21.5), 15 December 2006, at paras. 1-11 ["U.S. First Written Submission (21.5)"].

[4] U.S. First Written Submission (21.5), at paras. 3-10.

[5] *United States – Upland Cotton*, Appellate Body Report, at para. 763(c)(i), upholding the original panel's finding, at para. 8.1(g)(i).

[6] Second Written Submission of the United States, September 30, 2003, ["U.S. Second Written Submission"] at para. 115.

IV. LEGAL ANALYSIS

A. SCOPE OF PROCEEDING

12. The United States argues that the programmes are outside the scope of this proceeding because Article 21.5 applies only to "measures taken to comply with the recommendations and rulings" of the DSB. As the United States admits that it has not taken any measures to change these programmes, "Brazil may not in these Article 21.5 proceedings again make these claims against unchanged measures".[7]

13. The U.S. reading of Article 21.5 ignores the fact that the scope of an Article 21.5 proceeding mandates scrutiny of the overall effect of the measures taken to comply. A panel must "assess measures taken to comply in their full context, including how such measures are introduced into, and how they function within, the particular system of the implementing Member".[8] That context here necessarily includes the continued existence of measures the original panel and Appellate Body found to be causing serious prejudice.

14. Significantly, the Appellate Body has also found that measures at issue in an Article 21.5 proceeding could encompass not only positive acts, but also *omissions*.[9] The United States admits that it has done nothing respecting marketing loan payment and counter-cyclical payment programmes to remove the adverse effects or withdraw these subsidies, but that the repeal of Step 2 has been sufficient to constitute compliance with the serious prejudice recommendations and rulings of the DSB.[10] The United States argues that the original panel was considering the collective effect of U.S. subsidy programmes, and that it need do nothing with respect to the marketing loan payment and counter-cyclical payment programmes. Yet Article 7.8 of the *SCM Agreement* states that a finding of serious prejudice requires the non-complying Member to take appropriate steps to remove the adverse effect or withdraw the subsidy. The United States bears the burden of demonstrating that the adverse effects no longer exist as a result of taking no action to modify or withdraw the two programmes at issue and this Panel has clear authority to consider this lack of action in determining whether there is indeed compliance under Article 21.5.

B. ORDINARY MEANING OF "THREAT" IN PART III OF THE *SCM AGREEMENT*

15. Article 5 of the *SCM Agreement* prohibits adverse effects to the interests of other Members through the use of a subsidy; one such adverse effect is serious prejudice. Footnote 13 in turn specifies that "'serious prejudice to the interests of another Member' is used in this Agreement in the same sense as it is used in paragraph 1 of Article XVI of the GATT 1994, *and includes threat of serious prejudice*" (emphasis added). Article XVI:1 makes clear that a Member can cause, and also threaten, serious prejudice.

16. While the concept of threat may be expressed in various ways, it concerns an indication of something undesirable coming.[11] The use of the verb "threaten" in Article XVI:1 of the GATT 1994 indicates that the very existence of a programme, and not necessarily its application, could constitute an infringement of that provision. As the Appellate Body in this case has observed, the ordinary

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[7] U.S. First Written Submission (21.5), at para. 48.

[8] *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada, Recourse by Canada to Article 21.5*, Report of the Appellate Body, WT/DS257/AB/RW, adopted 20 December 2005, at para. 67.

[9] *Ibid.*, at para. 67.

[10] *See* U.S. First Written Submission (21.5), at paras. 1-11.

[11] *Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002, at 3251 ("threat").

meaning of "threaten" does not connote certainty, but relates to the likelihood of something happening in the future.[12]

17. Further analysis of the text of the *SCM Agreement* supports this ordinary meaning. Article 5 prohibits the use of a subsidy to the extent that such use causes, or threatens to cause, serious prejudice to the interests of another Member. "Subsidy" is defined in Article 1 of the *SCM Agreement*; a subsidy is deemed to exist if "a government practice involves […] *potential* direct transfers of funds or liabilities (e.g., loan guarantees)" and a benefit is thereby conferred.[13] In other words, the existence of a programme that has the *potential* to transfer funds, whether or not an actual transfer occurs, constitutes a subsidy pursuant to Article 1 of the *SCM Agreement*.[14] It follows that such a potential transfer could constitute a threat of serious prejudice.

18. The opening phrase of Article XVI:1 of the GATT 1994, refers to "any contracting party [that] grants or maintains any subsidy". As that article makes clear, it is not only the actual grant of a subsidy that allows for serious prejudice to be found. Merely *maintaining a programme* that mandates payments deemed to be a subsidy causing adverse effects may therefore cause serious prejudice, and indeed *will* cause serious prejudice when the specified market conditions arise.

19. Considering this, the U.S. proposition that the standard for threat of serious prejudice should be imported from Article 15.7 cannot be correct. Article 15.7 of the *SCM Agreement* concerns a different legal concept, namely the threat of material injury. Where a standard from another article or other agreement is to be used, the *SCM Agreement* identifies that standard.

20. This is evident through an examination of the notes to Article 5. Footnote 11 in Article 5(a), for example, states that "[t]he term 'injury to the domestic industry' is used here in the same sense as it is used in Part V". Footnote 12 in paragraph (b) states that "[t]he term 'nullification or impairment' is used in this Agreement in the same sense as it is used in the relevant provisions of GATT 1994, and the existence of such nullification or impairment shall be established in accordance with the practice of application of these provisions". Footnote 13, as quoted above, also incorporates a definition from the GATT 1994 into the *SCM Agreement*.

21. Neither Article 5 or 6 of the *SCM Agreement* set out a specific standard that is to be applied in an analysis of threat of serious prejudice. In other WTO agreements, as with Article 15.7, the standard applied when considering whether a threat of a particular deleterious result exists is set out in clear terms. For example, threat of serious injury in Article 4(1)(b) of the *Safeguards Agreement* means "serious injury that is clearly imminent […] based on facts and not merely on allegation, conjecture or remote possibility". The *Antidumping Agreement* specifies that "[a] determination of a threat of material injury shall be based on facts and not merely on allegation, conjecture or remote possibility. The change in circumstances which would create a situation in which the dumping would cause injury must be *clearly foreseen and imminent*" (emphasis added).

22. These examples support the conclusion that one must look to the specific language and context of an agreement to determine the standard to be applied to a given analysis. What is clear is that the scope of the term "threat" in Articles 5 and 6 of the *SCM Agreement* may be considerably broader than that contemplated in Article 15.7.

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[12] *United States - Upland Cotton*, Appellate Body Report, at para. 704.

[13] *SCM Agreement*, subparagraph 1.1(a)(1)(i) [emphasis added].

[14] As we understand the U.S. measures at issue, the terms of the "potential direct transfer" will necessarily result in a benefit to the recipient because that recipient would receive a financial contribution on terms more favourable than would otherwise be available to the recipient in the market. The nature of this benefit may vary, but could take the form of financial security provided by the very existence of the programmes.

23. This is consistent with the interpretation given by panels and the Appellate Body to other "threats". The Appellate Body reviewed the meaning of "threat of circumvention" in the context of the *Agreement on Agriculture* in this case.[15] It found that while "threaten" had a variety of possible meanings, Article 10.1 of the *Agreement on Agriculture* "is concerned not with injury, but rather with 'circumvention'". Given the ordinary meaning of "threaten", the phrase 'threaten[] to lead to ... circumvention' would imply that the export subsidies are applied in a manner that is 'likely to' lead to circumvention of a WTO Member's export subsidy commitments.[16] The Appellate Body did not import the standard of "clearly foreseen and imminent" into the standard for "threat" in the *Agreement on Agriculture*.[17] In fact, it emphasized that "threat" did not connote a sense of certainty and refers only to a likelihood of something happening.

24. That the meaning of threat is flexible is supported by two decisions concerning the consistency of the EC's sugar programme with Article XVI of the GATT 1994. In both *EC – Sugar (Australia)* and *EC – Sugar (Brazil)*, the panels found that the EC had structured its sugar programme so as to constitute a permanent source of uncertainty in world sugar markets, which given the facts of those cases, gave rise to a threat of serious prejudice in the sense of Article XVI:1.[18] Key to these findings was the lack of pre-established limitations on production, price or the amounts of exports in the Community system, very similar problems faced here by competitors to U.S. cotton farmers.[19]

25. It is not only the terms of the *SCM Agreement* read in context, but also the Agreement's very object and purpose that demonstrates that the standard for threat of serious prejudice may be distinct from that of threat in the case of material injury. In *Canada – Aircraft*, the panel noted that the object and purpose of the *SCM Agreement* could be summarised as "the establishment of multilateral disciplines 'on the premise that some forms of government intervention distort international trade, [or] have the *potential* to distort [international trade]'".[20]

26. As noted, the marketing loan and counter-cyclical programmes have the very real potential to distort international trade, and preventing the serious prejudice that will be caused when payments are made under these programmes is precisely what was intended by including Article 5 in the *SCM Agreement*. In its report, the original panel found that Part III of the *SCM Agreement* and Article XVI:1 of the GATT 1994 "expressly provides Members with a right to take action against serious prejudice which may not yet have occurred".[21] Further, the original panel found nothing in the text indicating that the right to take action against serious prejudice that may not yet have occurred is limited to a window of subsidies provided in the past but which cause serious prejudice in the future. If a Member were unable to bring an action against subsidies until these were *actually paid*, the Panel

[15] *United States – Upland Cotton*, Appellate Body Report, at paras. 696-719.

[16] *Ibid*., at para. 704.

[17] Similarly, in *India – Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*, Report of the Panel, WT/DS90/R, adopted 22 September 1999, India argued that the "threat of […] a serious decline in [a Member's] monetary reserves" in the context of Article XVIII:9 of GATT 1994 did not require an *imminent* threat of a serious decline in reserves, as does Article XII:2(a). In this regard, the Panel stated at para. 5.197 that their interpretation would not "introduce an additional condition to Article XVIII:9", by introducing the condition of imminence into the concept of "threat" in that Article.

[18] *See European Communities – Refunds on Exports of Sugar*, GATT Panel Report, adopted 6 November 1979, BISD 26S/290, at para. (h) of conclusion ["*EC – Sugar Exports I (Australia)*"] and *European Communities – Refunds on Exports of Sugar – Complaint by Brazil*, GATT Panel Report, adopted 10 November 1980, BISD 27S/69, at para. (h) of conclusion ["*EC – Sugar Exports (Brazil)*"].

[19] Brazil, in Section 8 of its First Written Submission, explains how those same factors are present in the U.S. programmes at issue and results in a permanent source of uncertainty in the world cotton market. Canada agrees with that analysis.

[20] *Canada – Measures Affecting the Export of Civilian Aircraft*, Report of the Panel, WT/DS70/R, adopted 20 August 1999, at para. 9.119 [emphasis added].

[21] *United States – Upland Cotton*, Panel Report, at para. 7.191.

reasoned, it would undermine the object in Part III of *preventing* adverse effects to a Member's interests.

27. The subsidy programmes at issue are mandatory when certain events take place, in this case when upland cotton prices reach a certain level. If a Member were obliged to wait until a payment was actually made to bring a complaint, then the adverse effects of the subsidy could never be prevented and the ability to defend against a "threat" of serious prejudice would be rendered inutile. The original panel's finding, that Part III of the *SCM Agreement* and Article XVI of the GATT 1994 must allow a Member to prevent the serious prejudice caused by the application of programmes such as marketing loan and counter-cyclical payments, is consistent with the inclusion of the words "maintain" in GATT Article XVI:1 and "potential" in Article 1.1(a)(1)(i) of the *SCM Agreement*.[22]

28. Whether as a consequence of the very architecture of the *SCM Agreement* – Part III concerns the adverse effects of subsidies in the context of multilateral action by Members, whereas Part V concerns the actions of domestic investigating authorities in countervailing duty actions – it is clear on its face that the standard for threat of serious prejudice in Part III is not circumscribed by a "clearly foreseen and imminent" standard.[23] And, in Canada's view, that "clearly foreseen and imminent" standard should not and indeed cannot legally be imputed to Part III simply because the word "threat" appears there.

V. CONCLUSION

29. Accordingly, Canada respectfully requests that the Panel find that the United States continues to use subsidies that threaten to cause serious prejudice, through its marketing loan and counter-cyclical programmes, in violation of Articles 5 and 6 of the *SCM Agreement*.

[22] *See* paras. 17-18 above on the use of "potential" and "maintain" in these articles.

[23] A legal term may be set out in various places in a WTO agreement without having the same meaning. See, for example, the Appellate Body's analysis of the term "like products" in *European Communities – Measures Affecting the Prohibition of Asbestos and Asbestos-Containing Products*, Report of the Appellate Body, WT/DS135/AB/R, adopted 5 April 2001. The Appellate Body reasoned at paras. 88-89 that as a term must be interpreted in light of the context and of the object and purpose of the provision at issue, it follows that the meaning of "like products" in Article III:4 need not be identical to, e.g., the meaning given the same term in Article III:2.

ANNEX A-6

THIRD PARTY SUBMISSION OF CHAD

(5 January 2007)

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TABLE OF CASES

Short Title	Full Case Title and Citation
US – Upland Cotton or the "Appellate Body Report"	Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R, adopted 21 March 2005.
US – Upland Cotton or the "Panel Report"	Panel Report, *United States – Subsidies on Upland Cotton*, WT/DS267/R, and Corr.1, adopted 21 March 2005, modified by Appellate Body report, WT/DS267/AB/R
Brazil – Aircraft (Article 21.5 – Canada)	Panel Report, *Brazil – Export Financing Programme for Aircraft – Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW, adopted 4 August 2000, as modified by the Appellate Body Report, WT/DS46/AB/RW, DSR 2000:IX, 4093
Canada – Aircraft	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377
Canada – Aircraft (Article 21.5 – Brazil)	Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/RW, adopted 4 August 2000, as modified by the Appellate Body Report, WT/DS70/AB/RW, DSR 2000:IX, 4315
EC – CVDs on DRAMs	Panel Report, *European Communities – Countervailing Measures on Dynamic Random Access Memory Chips from Korea*, WT/DS299/R, adopted 3 August 2005
Mexico – Corn Syrup (Article 21.5 – US)	Appellate Body Report, *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States – Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6675
United States – Oil Country Tubular Goods Sunset Reviews (Article 21.5 – Argentina)	Panel Report, *United States – Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina – Recourse by Argentina to Article 21.5 of the DSU*, WT/DS268/RW [not yet adopted]
US – Softwood Lumber VI (Article 21.5 – Canada)	Appellate Body Report, *United States – Investigation of the International Trade Commission in Softwood Lumber from Canada – Recourse by Canada to Article 21.5 of the DSU*, WT/DS277/AB/RW, adopted 9 May 2006

> *[O]ur countries are not asking for charity, neither are we requesting preferential treatment or additional aid. We solely demand that, in conformity with WTO basic principles, the free market rule be applied. Our producers are ready to face competition on the world cotton market – under the condition that it is not distorted by subsidies.*
>
> H.E. President Blaise Compaoré of Burkina Faso[1]

I. INTRODUCTION

A. BACKGROUND

1. On 21 March 2005, the Dispute Settlement Body (the "DSB") adopted the reports of the panel and the Appellate Body in the dispute *United States – Subsidies on Upland Cotton*.[2] These reports concerned a case brought by Brazil regarding various subsidies granted to United States cotton producers. In accordance with the findings in these reports and the DSB's recommendations and rulings, the United States was obliged, *inter alia*, under Article 7.8 of the Agreement on Subsidies and Countervailing Measures (the "*SCM Agreement*") either to withdraw subsidies that were found to cause serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement* or to remove the adverse effects caused by those subsidies.[3]

2. On 18 August 2006, pursuant to Article 21.5 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (the "DSU"), Brazil requested that the DSB establish a panel to determine whether the United States had complied with the rulings and recommendations of the DSB. The Panel was established upon Brazil's second request on 28 September 2006, and composed by the Director-General on 25 October 2006.[4] Argentina, Australia, Canada, Chad, China, the European Communities, India, Japan, New Zealand, and Thailand reserved their rights to participate in the Panel's proceedings as third parties.[5]

3. Chad appreciates the opportunity to present its views to the Panel in this written submission and at the meeting of the Panel with third parties, currently scheduled for 27 February 2007.

B. CHAD'S INTEREST IN THESE PROCEEDINGS

4. Chad is one of the very few least-developed countries ("LDCs") to have participated in a WTO dispute settlement proceeding since the organization was established in 1995. Chad participated in the original dispute in this case, and continues to participate in these proceedings, because of the critical importance of the cotton sector to Chad's economy and the ongoing damage to that sector caused by U.S. subsidies.

5. Chad notes that this dispute has arisen in the broader context of the commitment of WTO Members in the July Framework and reiterated at the Hong Kong Ministerial Conference to address cotton "ambitiously, expeditiously and specifically" with a view to achieving more ambitious

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[1] Address to the Trade Negotiations Committee, 10 June 2003, www.wto.org.
[2] Panel Report; Appellate Body Report.
[3] Panel Report, paras. 8.2(g)(i), 8.3(d).
[4] WT/DS267/31.
[5] *Ibid.*

reductions of trade-distorting domestic subsidies for cotton production.[6] While that commitment was made without prejudice to actions of the Dispute Settlement Body, it provides important context to guide the Panel's consideration of the issues before it. The protection of Chad's cotton industry is also consistent with the fulfilment of many of the Millennium Development Goals, in that it can assist in reducing poverty, improving health and reducing child mortality, and developing a global partnership for development, based on a rules-based trading system that addresses the special needs of least-developed countries, such as Chad.

6. As Chad has reiterated in the context of its Trade Policy Review to be held on 22-24 January 2007, cotton production in Chad affects approximately 3 million people, out of a total population of about 8.1 million.[7] The cotton-producing region of Chad is located in the southern part of the country, in an area covering about 127,000 square kilometres. Cotton is generally grown on small farms of usually no more than one or two hectares by farmers who rely on rain for irrigation and animals for traction when working the cotton fields during the sowing season.[8] Cotton exports are Chad's third largest export, accounting for 5 per cent of GDP, and representing 60 per cent of all non-oil export earnings.[9] Cotton is, therefore, one of Chad's main sources of income, and sustains the livelihood of a large portion of its population.[10]

7. As Chad explained in its report for its forthcoming Trade Policy Review, cotton is a strategic product that contributes not only to economic development but also social development.[11] Produced rurally on small farms, its positive effects on reducing poverty are felt most in those regions. Thus, cotton is "not only a source of revenue for these rural regions but also a tool for modernisation, diversification, and the financing of social activities and other needs of rural peasant societies".[12] These observations corroborate the findings of the Overseas Development Institute, which notes that:

> In a low-income economy where most of the poor live in rural areas, income from export crops is one of the best short-term measures to alleviate poverty. Smallholder cash-crop producers … spread [ ] the benefits to other poor households. Cotton is relatively labour intensive and may also generate employment. In African countries,

[6] *See* Doha Work Programme – Ministerial Declaration Adopted on 18 December 2005, WT/MIN(05)/DEC, para. 11.

[7] Trade Policy Review of Chad, Report by Government, WT/TPR/G/174, 11 December 2006, para. 28. According to the World Bank, there are roughly 400,000 farm households in the cotton-producing areas of Chad, of which about 60 per cent grow cotton. An average farm household has 5 to 6 people. *See* World Bank, *Chad Cotton Sector Reform: A Case Study on Poverty and Social Impact Analysis*, available at http://poverty.worldbank.org/files/13138_chadcottonreform.pdf.

[8] See Third Party Submission of Benin and Third Party Submission of Chad, Annex E-4 to the Panel Report.

[9] Trade Policy Review of Chad, Report by Government, WT/TPR/G/174, 11 December 2006, para. 28. See also P. Fortucci, *The Contributions of Cotton to Economy and Food Security in Developing Countries*, Food and Agriculture Organization of the United Nations (July 2002).

[10] As the WTO Secretariat has recently reported, "[a]griculture, mainly livestock breeding and cotton, is an activity of vital importance for Chad". Trade Policy Review of Chad, Report by the Secretariat, WT/TPR/S/174, 11 December 2006, pp. ix – x. Similarly, a United States agency has acknowledged the vital role played by cotton in Chad's agro-based economy: "over 80% of Chad's population relies on subsistence farming and livestock raising for its livelihood… Cotton, cattle, and gum arabic provide the bulk of Chad's non-oil export earnings". See The World Factbook, available at https://www.cia.gov/cia/publications/factbook/geos/cd.html.

[11] Trade Policy Review, Report of Chad, WT/TPR/G/174, 11 December 2006, para. 28.

[12] *Ibid*. (unofficial translation from the French).

> cotton production is concentrated in poorer regions so higher cotton incomes contribute to poverty reduction.[13]

8. Chad is one of the poorest countries in the world. In the United Nations Development Programme's Human Development Report of 2005, Chad is ranked as the 173rd out of 177 countries based on human development indicators that include life expectancy at birth, the infant mortality rate, and the maternal mortality ratio.[14] In these circumstances, it is imperative that the cotton farmers of Chad reap the benefits of the implementation of the DSB's rulings and recommendations in this dispute by the United States. Proper compliance would stabilise and increase the incomes of Chad's cotton farmers and help to develop the economy of Chad as a whole.

9. Full implementation by the United States of the DSB's recommendations and rulings in this case would have very significant benefits for Chad and the other Sub-Saharan African cotton-producing countries (Chad, Benin, Mali and Burkina Faso together comprise the "Cotton Four" or "C-4" countries). For example, a recent World Bank project study by Kym Anderson and Ernesto Valenzuela titled "WTO's Doha Cotton Initiative: A Tale of Two Issues"[15] specifically estimates what is at stake in terms of cotton production, trade, and economic welfare in Sub-Saharan Africa were the United States to comply *fully* with the rulings and recommendations of the DSB and remove the adverse effects of the non-repealed programmes.[16] The study finds that the removal of *all* cotton subsidies and import tariffs would boost global economic welfare by $283 million per year and would raise the price of cotton in international markets by almost 13 per cent. The authors note that:

> what is striking about the welfare effects is their distribution among developing countries… [e]specially noteworthy is the relatively large benefit bestowed on Sub-Saharan Africa of $147 million per year. This is driven by an estimated increase in Sub-Saharan African cotton output and value added of nearly one-third, and in the real value of the region's cotton exports of more than 50 per cent… That would raise Sub-Saharan Africa's share of global cotton exports from 12 to 17 per cent, and the share of all developing countries from 52 to 72 per cent.[17]

10. The potential impact of these welfare effects on incomes for cotton farmers in Chad cannot be understated: "[c]rucially they would rise by a huge 30 per cent in Sub-Saharan Africa and around 40 per cent in West Africa in particular – more than three-quarters of which is due to cuts in domestic support programs".[18] The World Bank Trade Note 27 of 30 March 2006 suggests that similar effects would be expected in the specific context of US compliance with the panel and Appellate Body Reports, stating that "the national welfare gains and boost to cotton farmers' incomes from partial reform are still concentrated in Sub-Saharan Africa and Central Asia".[19]

11. At the International Conference on Cotton: The Next Steps for Africa held in Washington D.C. on 26 October 2006[20], Professor Daniel Sumner presented findings regarding the

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[13] Overseas Development Institute (ODI) Annual Report 2005, page 10, available at http://www.odi.org.uk/annual_report/ar2005/ODI_AR2005.pdf

[14] Human Development Report 2005, published for the United Nations Development Programme.

[15] Kym Anderson and Ernesto Valenzuela, "WTO's Doha Cotton Initiative: A Tale of Two Issues", Development Research Group, World Bank, Washington DC, February 2006 (the "Anderson and Valenzuela study").

[16] *Ibid.*, pages 1–2.

[17] *Ibid.*, page 7.

[18] *Ibid.*, page 9.

[19] World Bank Trade Note 27, 30 March 2006, page 4.

[20] Daniel Sumner, Farm Programs and the Economies of LDC Cotton, Slide Show presented at the International Conference on Cotton: The Next Steps for Africa, Washington, D.C., 26 October 2006. Available

impact of the US subsidies on the C-4 countries. He found that the average gain from elimination of US subsidies on cotton would be a world price increase of about $0.05 per pound, which he calculates would "raise an annual revenue of about $75 to $100 million or more in the C-4 countries alone".[21] A World Bank economist has concluded that "the price prospects for cotton (and consequently the export shares of low-cost producers, including many African countries, could be improved considerably if developed countries substantially reduced or eliminated support and if the benefits of world price changes are fully transmitted to producers . . ."[22]

12. All of these changes would have an extremely positive effect on both the cotton sector and the economy as a whole in the C-4 countries. The C-4 countries' share of world cotton exports decreased from 10.05 per cent in 1998 to 8.57 per cent in 2002. It has continued to decrease since the original panel rulings to 7.35 per cent in 2005.[23] Chad's own share of cotton exports shows a similar trend, decreasing from 1.23 per cent in 1998 to 0.99 per cent in 2002 and 0.74 per cent in 2005.[24] These trends are in stark contrast to the United States' continuing *increasing* share of world cotton exports, which has grown from 18.27 per cent in 1998 to 39.24 per cent in 2002 and 39.72 per cent in 2005.[25]

13. Gobind Nankani, World Bank Vice President of the African Region, confirmed in a presentation at the October conference that after the difficult 2004/5 season, initial World Bank staff estimates for the 2005/6 ginning season show that production in the C-4 fell by 15 per cent, producer pricers fell by an average of 18 per cent, and the cotton sector's deficits remained at an estimated US$68 million for the four C-4 countries.[26]

14. At that same conference, the International Cotton Advisory Committee stated that:

> From the perspective of cotton producers in Africa and other developing countries, the key issue at hand is trade distorting agricultural subsidies that continue depressing world cotton prices, hurting millions of cotton farmers in Africa and elsewhere. The losses in income, employment, and foreign revenues far outnumber all of the assistance committed so far.[27]

15. The United Nations Development Programme's Human Development Report for 2005 highlights the effect of subsidies on cotton producers in poor countries, and concludes that in 2005, "the 20 000 cotton farmers in the United States will receive government payments in 2005 equivalent

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at: http://www.agritrade.org/events/speeches/CottonConference/Sumner.ppt (the "Sumner Presentation"). For full materials of the conference, see: http://www.ideascentre.ch/ConferenceWashington.htm

[21] Sumner Presentation, at slide 19.

[22] John Baffes, "The Cotton Problem," *World Bank Research Observer* 20(1): 109-44, Spring 2005, at page 132.

[23] Daniel Sumner, "U.S. Farm Programs and African Cotton: Discussion Paper Prepared for the 'International Conference on Cotton: The Next Steps for Africa' Washington, D.C., October 26, 2006", International Food & Agricultural Trade Policy Council Discussion Paper, Washington, DC. (forthcoming) (the "Sumner Discussion Paper"), Table 2 (sourced from: USDA FAS Production, Supply and Distribution Database, available at: http://www.fas.isda.gov/psdonline/psdDownload.aspx)

[24] *Ibid.*

[25] *Ibid.*

[26] Gobind Nankani, World Bank Vice President of the African Region, Development of the Cotton Sector in West and Central Africa, Slide Show at the International Conference on Cotton: The Next Steps for Africa, Washington, D.C., 26 October 2006, available at http://www.agritrade.org/events/speeches/CottonConference/Nankani.ppt.

[27] International Cotton Advisory Committee, The Importance of Cotton in Africa, presentation at the International Conference on Cotton: The Next Steps for Africa, Washington, D.C., 26 October 2006, available at http://www.agritrade.org/events/speeches/CottonConference/Townsend.pdf

to the market value of the crop and more than US aid in Sub-Saharan Africa."[28] The report also notes that "subsidies [of the order of the US subsidies] are reminiscent of the state planning systems that characterized the former Soviet Union".[29]

16. In these circumstances, it is evident that the proper implementation of the DSB's recommendations and rulings is of paramount importance to Chad and its fellow C-4 countries, which are some of the most vulnerable economies in the world. It is of critical importance to these countries and, indeed, to the multilateral trading system as a whole, that this compliance Panel carefully and stringently review the measures taken by the United States to comply with those recommendations and rulings to ensure that the rules governing the provision of subsidies are properly applied and followed.

17. As explained in this submission, and in more detail in Brazil's first written submission[30], the United States subsidies at issue in this dispute have had and continue to cause significant price suppression. This price suppression has an adverse impact on Chad's cotton farmers and on Chad's economy as a whole. And, as Brazil argues in its first submission, and Chad maintains below, the United Sates has not properly implemented the DSB recommendations and rulings regarding the adverse effects of these subsidies.

18. In assessing the impact of these subsidies on Chad, and the arguments that Chad makes in these proceedings, Chad requests that the Panel take note of Article 24 of the DSU, which states that: "[a]t all stages of the determination of the causes of a dispute, and of dispute settlement procedures involving a least-developed country Member, particular consideration shall be given to the special situation of least-developed country Members". For the reasons explained above, Chad's reliance on its cotton industry to generate exports and fight poverty constitutes just such a special situation. The Panel should give due consideration to this special situation by making recommendations and rulings that will lead to a competitive world cotton market that is not distorted by WTO-inconsistent subsidies.

II. LEGAL ARGUMENT

A. The United States has not taken steps to implement the rulings and recommendations of the DSB

19. The original panel found that the effect of several mandatory price-contingent U.S. subsidy programmes, including user marketing (or "Step 2") payments, marketing loan payments and counter-cyclical payments, caused significant price suppression in the world market for upland cotton, and thereby caused adverse effects to Brazil, in violation of Articles 5(c) and 6.3(c) of the *SCM Agreement*.[31] In its implementation of the DSB recommendations and rulings, however, the United States merely discontinued the Step 2 programme as of August 2006, while leaving unchanged the marketing loan and counter-cyclical payments.[32] As explained in more detail below, however, the

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[28] Human Development Report 2005, page 132.

[29] *Ibid.*, page 131.

[30] First Written Submission of Brazil to the Panel, 17 November 2006 ("First Written Submission of Brazil").

[31] Panel Report, para. 8.1(g)(i).

[32] See Exhibit Bra-435 (Deficit Reduction Act of 2005, U.S. Public Law 109-171, Section 1103, available at http://www.access.gpo.gov/nara/publaw/109publ.html). The United States Congress bill that repeals the Step 2 subsidy program for upland cotton was signed into law on 8 February 2006, and took effect on 1 August 2006. See Minutes of DSB Meeting, WT/DSB/M205, 17 February 2006, para. 92 and Exhibit Bra-441 ("House approves Byrd repeal, elimination of step 2 cotton program", Inside US Trade, 3 February 2006).

Step 2 programme accounted for, at most, one seventh of the aggregate subsidies to U.S. cotton production. Hence, the vast majority of the benefits of implementation were expected to come from the termination of the domestic support programmes.

20. Chad recalls that Article 7.8 of the *SCM Agreement* requires that the "Member granting or maintaining [any subsidy that has resulted in adverse effects to the interest of another Member] shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy".

21. Chad submits by simply ending Step 2 payments and leaving in place the other programmes found to cause adverse effects, the United States cannot be found either to have withdrawn the subsidies or to have removed the adverse effects thereof.

1. The United States has not properly implemented the panel's findings regarding the Marketing Loan and Counter-Cyclical Payment Programmes

22. It is undisputed that the marketing loan and counter-cyclical payment programmes have not been withdrawn. To the contrary, the United States argues that these programmes were not subject either to a finding of WTO inconsistency or any DSB recommendations.[33] The United States requests the Panel to find that the marketing loan and counter-cyclical payment programmes are not measures to which the recommendations and rulings of the DSB were addressed and, therefore, that these measures are not within the scope of the present proceedings.[34]

23. Chad disagrees with the United States' interpretation of the original panel's findings and the DSB recommendations and rulings. The original panel found that "the effect of the mandatory price-contingent measures" was significant price suppression within the meaning of Article 6.3(c) that constituted serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.[35]

24. The panel clearly described the measures at issue as including the "legislative and regulatory provisions currently providing for the payment of measures" including marketing loan and counter-cyclical programme payments.[36]

25. In its analysis of Brazil's claims under Articles 6.3(c) and 5(c) of threat of serious prejudice regarding the same measures, the panel also stated that there were "two main measures providing for the payment of the United States subsidies in question," which it described as the "FRSI Act of 2002 and implementing regulations" and "legislation providing for crop insurance subsidies prior to and since MY 2002."[37] The panel explained the consequences of its findings of present serious prejudice regarding these measures as follows:

> Because the Panel's 'present' serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002, the *United States is obliged to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice finding.* We recall that, pursuant to Article 7.8 of the *SCM Agreement*, the United States is under

[33] First Submission and Request for Preliminary Rulings of the United States of America, 15 December 2006 (the "U.S. First Submission"), para. 37.
[34] *Ibid.*, para. 44.
[35] Panel Report, paras. 7.14.16, 8.1(g)(i).
[36] *Ibid.*, para. 7.1107(ix).
[37] *Ibid.*, para. 7.1498.

> an obligation to 'take appropriate steps to remove the adverse effects or … withdraw the subsidy.'[38]

26. Thus, the panel clearly considered that its findings regarding "present" serious prejudice applied not just to payments, but to the statutory and regulatory framework of the FSRI Act of 2002 and its implementing regulations.

27. Moreover, the panel relied on the scope of its findings regarding "present" serious prejudice to decline to address Brazil's claims of threat of serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*:

> We consider that, upon *required implementation by the United States of this Panel's prohibited subsidy findings and present serious prejudice findings*, the basket of measures in question may be so significantly transformed or manifestly different from the measures that are currently in question that it is not necessary or appropriate to address Brazil's claims of threat of serious prejudice.[39]

28. Thus, the original panel clearly considered that its findings included not simply the payments themselves under the marketing loan and counter-cyclical payment programmes, but also the statutory and regulatory measures under which those payments were mandated.

29. The United States' arguments that the statutory and regulatory aspects of these measures were not covered by the Panel's findings are twofold. First, the United States argues that the panel's findings in paragraph 8.1(g)(i) of its report referred to "payments" not "programs" in the phrase between dashes. The United States' argument ignores that the panel described the payments at issue as "mandatory." This description necessarily implies that the measure at issue was not limited to the actual payments themselves, but included the statutory and regulatory framework that made those payments "mandatory." Accordingly, Chad does not consider the panel's failure to use the word "programmes" in paragraph 8.1(g)(i) of its report to be sufficient grounds to ignore the panel's description of the measures at issue and the Panel's explanation of what steps it considered necessary to implement quoted above.

30. Second, the United States argues that the panel did not address Brazil's *per se* or "as such" claims regarding these programmes, or Brazil's claims regarding threat of serious prejudice, and, therefore, the Panel's findings were strictly limited to the payments themselves. However, Brazil is not precluded from pursuing before this compliance panel claims regarding the threat of serious prejudice that the original panel declined to address.[40] These claims raise substantially the same issues regarding the statutory and regulatory framework for these programmes as Brazil's claims regarding the implementation of the panel's findings regarding present serious prejudice.

31. The United States' argument appears to confuse the issue of whether a statutory provision is challenged "as such" with the altogether separate issue of whether a statutory provision mandating certain payments can be found to cause serious prejudice. Brazil's claims before the original panel were that these payments, including the "legislative and regulatory provisions currently providing for the payment[s]" were actually causing serious prejudice. In other words, these claims were "as applied" claims regarding measures that included legislative and regulatory provisions. The distinction sometimes made in WTO proceedings between "as such" and "as applied" claims does not

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[38] *Ibid.*, para. 7.1501 (original footnote omitted) (emphasis added).

[39] *Ibid.*, para. 7.1503 (emphasis added).

[40] See, *e.g.*, Panel Report, *United States – Oil Country Tubular Goods Sunset Reviews (Article 21.5 – Argentina)*, paras. 7.90-7.94.

mean that statutory or regulatory provisions cannot be challenged on an "as applied" basis or that "as applied" claims are necessarily limited to the payments themselves to the exclusion of measures mandating those payments. Where a party includes statutory or regulatory measures in an "as applied" claim, as Brazil did before the original panel, implementation of the panel's findings with respect to that claim cannot be limited to one aspect of the measure (the payments) to the exclusion of other aspects (the governmental mechanisms whereby the payments are made).

32. For these reasons, the Panel should reject the United States' arguments that the marketing loan and counter-cyclical payment programmes are not within the scope of this proceeding.

33. The United States' failure to take implementing measures regarding the marketing loan and counter-cyclical payment programmes is within the scope of these proceedings. As explained above, the original panel's findings covered those programmes. Article 21.5 review includes both measures taken to implement and a *failure* to implement. In *U.S. – Softwood Lumber VI (21.5)*, the Appellate Body confirmed that "[t]he word "existence" suggests that measures falling within the scope of Article 21.5 encompass not only positive acts, but also *omissions*."[41] Thus, where an implementing Member fails to adopt "measures taken to comply" within the implementation period, it has made a failure or omission enabling a panel under Article 21.5 to conclude that no measures "exist" to implement the recommendations and rulings of the DSB.

34. As the only action undertaken by the United States was the repeal of the Step 2 programme on 1 February 2006 with effect from August 2006, it is clear that the United States has not withdrawn or amended the marketing loan or counter-cyclical payment programmes found to be inconsistent with the United States' WTO obligations.

2. The United States has not removed the adverse effects of the Marketing Loan and Counter-Cyclical Payment Programmes

35. As noted above, the United States has not taken any steps to address the adverse effects caused by the marketing loan and counter-cyclical payments.

36. Moreover, the withdrawal of the Step 2 payments cannot be said to have removed the adverse effects of the marketing loan and counter-cyclical payments.

37. The vast majority of the price suppression and adverse effects caused by the impugned U.S. programmes was and continues to be caused by the marketing loan and counter-cyclical payment programmes, rather than the Step 2 payments. The Anderson and Valenzuela study discussed above confirms this.[42] The study underlines that the repeal of the Step 2 programme is equivalent, at best, to "a one-seventh reduction in the aggregate subsidy to US cotton production" and, if the support were re-instrumented to direct production subsidies, "there would effectively be no global market impact of the repeal".[43] In contrast, if the counter-cyclical payment and marketing loan programmes were to be counted as part of the US amber box measures, they would be required to be cut by US$1 billion, which would be "more than twice the amount associated with repealing the Step 2 program".[44]

38. These findings accord with those of Daniel Sumner who has also provided estimates of the effects of individual programmes. He notes that the Step 2 programme alone accounts for only about 15 per cent of the total subsidy impact, however "the major farm bill programs, marketing loans and

[41] See Appellate Body Report, *U.S. – Softwood Lumber VI (Article 21.5 -- Canada)*, para. 67.
[42] Anderson and Valenzuela study, page 10.
[43] *Ibid.*
[44] *Ibid.*

counter-cyclical payments, account for most of the remaining subsidy effect".[45] Professor Sumner concludes that if the US were to implement fully the recommendations and rulings of the DSB by removing these programmes, LDCs would benefit from substantial price and production increases would be available to least-developed countries.[46]

39. Thus, the US domestic support programmes, rather than export subsidies under the Step 2 programme, are most detrimental to Chad. Using the GTAP database and model, the Anderson and Valenzuela study demonstrates that over 80 per cent of the benefits from removal of all cotton subsidies and import tariffs will come from cutting domestic support programmes rather than export subsidies which will "contribute almost none of the global benefits of reform".[47]

40. Chad submits that in addition to the effect of the subsidies on Brazil, the US subsidies continue to cause adverse effects within the meaning of Article 5(c) and 6.3 of the *SCM Agreement* on the world market for upland cotton, and, consequently, to the interests not just of Brazil of Chad and other cotton-producing African countries.

41. The original panel has already found that:

> [T]he effect of the mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments – is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.[48]

42. Chad submits that the findings and analysis of the original panel continue to be relevant to this analysis because these proceedings are part of a "continuum of events".[49] The Appellate Body in *United States – Softwood Lumber VI (21.5)* stated that a panel operating under Article 21.5 of the DSU cannot perform its task of "in abstraction from the measure that was the subject of the original proceedings",[50] and that "doubts could arise about the objective nature of an Article 21.5 panel's assessment if, on a specific issue, that panel were to deviate from the reasoning in the original panel report in the absence of any finding in the underlying evidence."[51] As the Appellate Body stated:

> Article 21.5 panels can be expected to refer to their original panel reports, in particular, when matters before them are closely related to the matters before original panels.[52]

43. This reasoning also applies to this dispute. The claims of serious prejudice in this dispute as they relate to the marketing loan and counter-cyclical payments involve the same subsidy programmes that were at issue before the original panel. As the United States has not changed those measures that

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[45] Sumner Discussion Paper, page. 20.

[46] *Ibid.*

[47] "[E]xport subsidy removal would contribute almost none of the global benefits of reform, and cotton tariff removal would account for only one-nineth of the global gain, with the other eight-nineths due to cutting domestic support programs", p. 8. See also World Bank Trade Note 27, 30 March 2006, p. 2.

[48] Panel Report, para. 8.1(g)(i).

[49] See Appellate Body Report, *Mexico – Corn Syrup* (Article 21.5 – US), para. 121.

[50] Appellate Body Report, *United States – Softwood Lumber VI (21.5)*, para. 102.

[51] *Ibid.*, para. 103.

[52] *Ibid.*, para. 105. See also Appellate Body Report, *Mexico – Corn Syrup* (Article 21.5 – US), para. 121

were found to cause serious prejudice by the original panel, this Panel should rely on the factual and legal conclusions concerning the existence, nature and potential for price suppression of those measures in the original panel report. Chad refers the Panel to the relevant findings of the original panel on those matters.[53]

44. As noted above, the marketing loan and counter-cyclical payments account for the *vast majority* of the adverse effects identified by the original panel. The failure to implement the original panel's findings with regard to these subsidies has therefore deprived cotton exporters such as Chad of the benefits of the panel's findings and has resulted in the ongoing harm to a critically-important sector of Chad's vulnerable economy described above. In these circumstances, taking note of Chad's special situation, this Panel should follow the reasoning of the original panel and find that the adverse effects continue, and have not changed. Chad, therefore, supports the arguments of Brazil that the marketing loan and counter-cyclical payment programmes under the FSRI Act of 2002 *alone* cause present serious prejudice and requests the Panel to find accordingly.[54]

45. Moreover, as explained above in paragraphs I.B.12 and I.B.13, and as Brazil notes in its first written submission to the Panel, the price effects of the U.S. subsidies have continued and, indeed, gotten worse since the original panel's rulings. Chad and the other C-4 countries have continued to lose market share in cotton exports, even while the United States' market share continues to increase. In addition, C-4 cotton production and producer prices have continued to decrease substantially, by 15 and 18 per cent respectively in 2005/05. Brazil observes that, West and Central African countries' share of world production declined from 5.15 per cent in MY 2002 to 3.85 per cent in MY 2005 – a 25 per cent decrease.[55] The region's share of world exports declined from 13.51 per cent in MY 2002 to 11.10 per cent in MY 2005. Indeed, the West and Central African countries share of world exports in MY 2005 was the lowest that it has been in the past 10 years.[56]

46. For these reasons, therefore, Chad supports Brazil's claim that the "non-repealed price-contingent U.S. marketing loan and counter-cyclical payment programs under the FSRI Act of 2002 cause present serious prejudice in the form of significant price suppression in the world market for upland cotton, and an increase in the U.S. world market share, in violation of Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*", and requests the Panel to find accordingly.[57]

3. Payments to be made in Marketing Year 2006 threaten to cause serious prejudice

47. Chad also supports Brazil's claim that despite the repeal of the Step 2 program, the marketing loan and counter-cyclical payments mandated under the FSRI Act of 2002 to be made in MY 2006, and beyond, cause a threat of serious prejudice within the meaning of Articles 5(c) and 6.3(c) as well as footnote 13 of the *SCM Agreement*.

48. As established by the original panel, the marketing loan and counter-cyclical payment programs are mandatory, have guaranteed high levels of U.S. planted acreage, production and exports and have caused significant price suppression. The continued granting of these subsidies, which is

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[53] See Panel Report, paras. As read with the Appellate Body Report, para.

[54] First Written Submission of Brazil, para. 47 *et seq*.

[55] Compare West and Central Africa production (Exhibit Bra-450 ("Cotton: World Statistics," ICAC, September 2006, p. 26 and p. 28) with world upland cotton production (Exhibit Bra-447 (Upland Cotton Supply and Use)).

[56] Compare West and Central Africa exports (Exhibit Bra-450 ("Cotton: World Statistics," ICAC, September 2006, p. 56 and p. 58) with world upland cotton exports (Exhibit Bra-447 (Upland Cotton Supply and Use)).

[57] First Written Submission of Brazil, para. 6.

mandated by law, constitutes a continuing threat of significantly suppressed world market prices for developing country cotton producers, and will continue until these subsidy programs are repealed or significantly amended.

49. Chad refers to Brazil's arguments and supporting evidence on this claim, and asks the Panel to find that these subsidies cause present serious prejudice, and cause a threat thereof, in violation of Articles 5(c), 6.3(c) and footnote 13 of the *SCM Agreement*.

B. THE PANEL SHOULD ANALYSE THE EXPORT CREDIT GUARANTEE PROGRAMMES UNDER ARTICLE 1.1(B) OF THE *SCM AGREEMENT*

50. Chad also supports the arguments of Brazil regarding the United States' implementation of the recommendations and rulings of the DSB regarding the export credit guarantee programmes ("ECGs") maintained by the Commodity Credit Corporation.[58]

51. Chad considers that it is particularly important that this Panel interpret strictly the provisions of the *SCM Agreement* and the *Agreement on Agriculture* governing ECGs. As a practical matter, only developed country governments can effectively provide ECGs to promote their exports. As a previous panel has noted:

> [T]hrough export credit guarantees, governments can effectively make their borrowing rates available to borrowers. However, the borrowing rates for developed country governments are generally lower than those of developing country governments. As a result, developing country Members . . . could never meet the financing terms secured by developed country Members through government guarantees.[59]

52. That observation applies *a fortiori* to a LDC such as Chad. An ECG from an AAA-rated government enables exports from that country to be made on financing terms normally available to borrowers with a AAA credit risk. Thus, the purchasers of goods backed by U.S. ECGs benefit from the United States government's credit rating, giving a competitive advantage to U.S. exporters. In addition, ECGs are a relatively inexpensive means for developed countries to support their exports in that they involve no immediate cash outlay.

53. In contrast, countries like Chad do not have strong enough credit ratings to be able to provide competitive ECGs. They also lack the resources to be able to provide ongoing funding for such programmes. Thus, developing country Members, and particularly LDCs, face permanent structural disadvantages compared to developed country Members in providing export credit.

54. ECGs are subject to the disciplines of the *SCM Agreement*. Panels and the Appellate Body have found that ECGs may be inconsistent with the *SCM Agreement* if: (a) a government ECG is offered on terms better than those available to the recipient for an equivalent guarantee that could have been obtained in the marketplace (thereby conferring a benefit within the meaning of Article 1.1(b) of the *SCM Agreement*)[60]; (b) a government ECG improves the terms of an underlying loan compared to the terms that could have been secured in the marketplace without the government ECG (based on Article 14(c) of the *SCM Agreement*)[61]; and (c) a government ECG program charges

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[58] First Written Submission of Brazil, page 130 *et seq.*

[59] Panel Report, *Brazil – Aircraft (Article 21.5 – Canada)*, footnote 98. See also Panel Report, *Canada – Aircraft (Article 21.5 -- Brazil)*, para. 5.136.

[60] Panel Report, *EC – CVDs on DRAMs*, para. 7.189.

[61] *Ibid.*

premium rates that are inadequate to cover the long-term operating costs and losses of the programmes (based on item (j) of the Illustrative List of Export Subsidies included as Annex I to the *SCM Agreement*).[62]

55. The structural disadvantages faced by Chad and other LDCs with respect to ECGs do not, of course, affect the right of other WTO Members to provide ECGs consistent with the disciplines described above. However, the special situation of LDCs as a result of these disadvantages should provide important factual context for the current Panel in its interpretation of the relevant provisions of the *SCM Agreement* and its evaluation of the United States' measures.

56. In particular, the Panel should not limit its review of the U.S. ECGs to the question of whether the rates at which ECGs are provided are inadequate to cover the long-term operating costs and losses of the programme within the meaning of item (j) of the Illustrative List. In addition, the Panel should carefully review whether the U.S. ECGs confer a "benefit" within the meaning of Article 1.1(b) of the *SCM Agreement* as interpreted by the Appellate Body in *Canada – Aircraft*.[63]

III. CONCLUSION

57. As Chad has stated above, the Panel should, under DSU Article 24, consider the interests of LDCs such as Chad in this proceeding. Such consideration is particularly appropriate where, as here, WTO-inconsistent measures taken by an affluent developed country WTO Member continue to cause serious harm to an important subsistence farming sector in the economy of some of the very least-developed countries in the world.

58. In requesting the Panel's careful consideration of the special situation of Chad and its fellow C-4 countries in this proceeding, Chad does not ask the Panel in any way to bend the rules of the WTO agreements to suit Chad. Instead, to paraphrase former WTO Deputy Director-General Dr. Kipkorir Rana, Chad simply asks the Panel to ensure, through a careful review of the evidence and rigorous application of the law, that the relevant WTO rules and disciplines are fully applied to the cotton sector so that a fair and market-oriented system can prevail, thereby eliminating wasteful subsidies that cause substantial harm to the poorest WTO Members.[64]

59. In Chad's view, Brazil has produced compelling arguments and evidence to show that the United States price-contingent subsidy programs supporting upland cotton under the FSRI Act have not been withdrawn or changed in any significant way. Brazil has also shown that overproduction and excess exports, along with significantly suppressed world market prices for upland cotton, have continued following the adoption of the reports of the original panel and the Appellate Body in this dispute. As explained above, Chad's own experience confirms the evidence submitted by Brazil.

60. Accordingly, Chad requests that the Panel make the findings requested in paragraph 462 of Brazil's First Submission and the recommendations requested in paragraph 463 of that submission.

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[62] See, *e.g.*, Appellate Body Report, paras. 672 and 674; Panel Report, paras. 7.867 and 7.869.

[63] Appellate Body Report, *Canada –Aircraft*, paras. 152 *et seq.*

[64] "[Benin, Burkina Faso, Mali and Chad] do not ask for aid, which is the World Bank's remit, nor do they make political appeals that belong to the United Nations. They have just asked that WTO rules and disciplines apply also in sectors of interest to the poor – that a fair and market-oriented system be established in agriculture and that rich countries' wasteful export and production subsidies be abolished and cease to undermine their comparative advantage." Former WTO Deputy Director-General Dr. Kipkorir Rana, Address given to the Second East African Business Summit, "The Multilateral Trading System: Why East Africa Must Remain Engaged" 18-21 September 2003, www.wto.org.

ANNEX A-7

THIRD PARTY SUBMISSION OF PEOPLE'S REPUBLIC OF CHINA

(5 January 2007)

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1. INTRODUCTION

1. China appreciates this opportunity to present its views on implementation measures by the United States (the US) in accordance to the ruling and recommendations adopted by the Dispute Settlement Body ("DSB") in the original proceedings.

2. Pursuant to Article 10 of *Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"),* China hereby makes its Third Party Submission.

3. In this submission, China will focus on the following issues:

1) Whether the item (j) of the Illustrative List of SCM Agreement constitutes the complete basis for analysis of GSM102 as amended;

2) Whether the ML/CCP payment "programs" are outside the scope of this proceeding;

2. ARGUMENTS

2.1 Whether the item (j) of the Illustrative List of SCM Agreement constitutes the complete basis for analysis of GSM102 as amended

4. In its submission, Brazil demonstrates that under Article 1.1 and 3.1(a) of the SCM Agreement, GSM 102 ECGs are "financial contributions" that confer "benefits", and that these subsidies are contingent in law on export performance.[1] Furthermore, Brazil submits a alternative claim under item (j) that the program continues to constitute an export subsidy, since fees continue to be insufficient to cover the long-term operating costs and losses of the program.[2]

5. The US rebuts Brazil's approach by claiming it would lead to the fatally flawed result that a measure that was specifically found to fall outside the definition of an export subsidy could then be found to be an export subsidy. The US asserts that "it is item (j) that provides the basis for assessing whether or not GSM-102 export guarantees are export subsidies within the meaning of Article 3.1(a) and 3.2 of the SCM Agreement."[3] In addition, the US appears to claims that, "in the case of measures identified in the Illustrative List, it is the specific provisions of the Illustrative List – and not the general subsidy provisions in the Articles 1.1 and 3.1(a) – that govern when the measures may be considered export subsidies."[4] In sum, it appears that the US argued a *contrario* interpretation of item (j) in order to justify its amended GSM-102 program.

6. In this regard, China believes that the finding of the panel in *Korea-Measures Affecting Trade in Commercial Vessels* can provide useful guidance. In discussions concerning the item (j) defense, the panel pointed out that "Item (j) contains no such affirmative statement. Item (j) merely describes certain circumstances in which particular programs shall constitute export subsidies. Since item (j) therefore falls outside the scope of footnote 5, item (j) does not provide a basis on which to find that measures do not constitute prohibited export subsidies".[5] The panel further concluded that "on its face, item (j) defines certain circumstances in which export credit guarantee programs <u>are</u> export subsidies. Item (j) simply does not address export guarantee programs that <u>do</u> cover their long-term

[1] Brazil First written Submission, para. 361.
[2] Brazil First written Submission, para. 362.
[3] *See* First Submission and Request For Preliminary Rulings of The United States of America, para. 66.
[4] *Ibid*, para. 65.
[5] Panel Report on *Korea-Measures Affecting Trade in Commercial Vessels,* para. 7.178

operating costs and losses."[6] Accordingly, the panel found that *a contrario* interpretation of item (j) was not permissible.

7. Hence, item (j) is only a shortcut to determine an export credit guarantee constitutes an export subsidy when the guarantee does not cover its long-term operating costs and losses. However, it is not a defense clause. When a guarantee does cover its long-term operating costs and losses, it is still possible that the guarantee constitutes an export subsidy. Namely, if requirements of item (j) are not met by a measure, the panel still needs to examine whether or not the measure is consistent with Article 1 and 3 of SCM, specifically, whether it constitutes a financial contribution that confers benefits. In China's view, the scope of export subsides in the meaning of Article 1 and 3 of SCM is broader than scope of item (j) of the illustrative list. The complainant may raise a *prima facie* case of export subsidy either by claiming an illustrative list violation or Article 1 and 3 of SCM violations. Nevertheless, non-existence of the illustrative list violation does not mean that it also consistent with obligations under Article 1 and 3 of SCM.

8. Thus, in the opinion of China, the US's approach of proceeding from item (j) is incomplete. It is the provisions in the Agreement of Agriculture and SCM Agreement *plus* item (j) in the Illustrative List rather than the item (j) itself only can be taken as the complete basis for analyzing the nature of GSM 102 programs. Even if the US could prove GSM 102 programs' premium could cover the long-term operating costs and losses of the programs, it still has to prove that it is consistent with the discipline of export subsidy specified in the Articles 1 and 3.1(a) of SCM Agreement and the relevant provisions in AoA.

2.2 Whether the ML/CCP payment "programs" are outside the scope of this proceeding

9. Brazil requests that the compliance panel to determine that the US has failed to comply fully with its obligation, under Article 7.8 of SCM Agreement, to "withdraw the subsidy" or to "remove the adverse effects" with respect to the US price-contingent subsidy programs.[7] Brazil believes that the new basket of measures providing support to the US upland cotton producers (*i.e.*, the marketing loan and counter-cyclical payment) continue to cause serious prejudice as well as a threat of serious prejudice to the interests of Brazil.

10. On the other hand, the U.S. argues that ML/CCP *Programs* are outside the scope of this proceeding.[8] In the opinion of the U.S., (1) "the marketing loan and counter-cyclical payment *programs* were not subject either to any finding of WTO-inconsistency or any DSB recommendations",(emphasis added)[9] since "Brazil clearly distinguished between claims against *programs per se* and claims against *specific payments under the programs*."(emphasis added)[10]; and (2) since ML/CCP Programs have not been changed, in response to DSB recommendations and rulings or otherwise, they are not "measures taken to comply".[11]

11. China can not endorse the position of the US that the US needs to do nothing concerning the ML and CCP programs.

12. In the first place, contrary to what the US asserted in its Submission, DSB did make rulings and recommendations in respect to ML/CCP programs in many occasions in the Panel Report, (1) the

[6] Panel Report on *Korea-Measures Affecting Trade in Commercial Vessels*, para. 7.203
[7] *Ibid*, para. 29
[8] *See* U.S. First Written Submission, para. 44.
[9] *Ibid*, para. 37.
[10] *Ibid*, para. 32.
[11] *Ibid*, para. 45.

panel found as one of the "measure at issue" the "legislative and regulatory provisions currently providing for the payment of measures," including that of ML and CCP.[12] This shows that "legislative and regulatory provisions" of ML/CCP are measures subject to rulings/findings by the panel. (2) in discerning the specificity of the measures at issue, the panel found that "a textual analysis of 'the legislation pursuant to which the granting authority operates' leads us to conclude that such subsidies are 'specific' within the meaning of Article 2.1(a)."[13] This clarifies that the panel did make findings to some extent regarding to the legislation authorizing ML/CCP subsidies. (3) in establishing the causal links between the US subsidies and the significant price suppression, the panel found that marketing loan program payments and CCP payments, among others, are *directly linked to* world prices for upland cotton, thereby insulating US producers from low prices, and that *the structure, design and operation of these measures* constitute evidence supporting a causal link with significant price suppression.[14] These are explicit descriptions of the ML/CCP programs in the sense that "directly linked to world price" is a mechanism by which a subsidy payment is to be made, rather than the payment per se, and that the phrase "*structure, design and operation of these measures*" is clearly synonymous to the programs. In short, these findings clearly show that the original panel had made rulings on the ML/CCP programs.

13. In addition, in regard to its findings on "threat of" serious prejudice, the Panel concluded by ruling explicitly that the United States is obliged to take action concerning its *present statutory and regulatory framework* as a result of our 'present' serious prejudice finding."(emphasis added)[15] In making its findings on Brazil's "claims of per se inconsistency", the original Panel found that "In light of our findings above in Sections VII:E, F, G and H, we do not believe that it is necessary to address *Brazil's per se claims relating to these measures* under Articles 5(c) and 6.3(c) and (d) of the SCM Agreement and Articles XVI:1 and XVI:3 of the GATT 1994."(emphasis added)[16] The quotations show that the panel assumed the statutory and regulatory framework of the US should be changed and refrained itself from make further elaboration in this regard.

14. One step backwards, assuming that the original panel did not make any recommendations in respect to ML/CCP *programs* on the basis that it adopted judicial economy on Brazil's per se claim, the US still needs to take measures to remove adverse effects caused by those subsidies including ML and CCP programs.

15. Another claim by the US with regard to scope of these compliance proceedings is that "Brazil may not in these Article 21.5 proceedings again make these claims against unchanged measures."[17] In this regard, China recalls that in paragraph 8.1(g)(i) of its report, the original panel found that " the effect of the mandatory price-contingent United States subsidy measures – marketing loan program payments, user marketing (Step 2) payments, MLA payments and CCP payments – is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*." The recommendations and rulings of the DSB obliged the United States, under Article 7.8 of the *SCM Agreement*, to remove the adverse effects caused by these subsidies, or to withdraw the subsidies.[18]

[12] Panel Report on *U.S. – Upland Cotton*, para. 7.1107.
[13] *Ibid*, para. 7.1146.
[14] *Ibid*, para. 7.1349.
[15] *See* Panel Report, *U.S. – Upland Cotton*, para. 7.1501.
[16] Panel Report, *U.S. – Upland Cotton*, para. 7.1511.
[17] US First Submission, para. 48.
[18] Panel Report, *U.S. – Upland Cotton*, para. 8.3(d). Brazil recalls that the Panel and Appellate Body reports were adopted by the DSB on 21 March 2005.

16. As submitted by Brazil and admitted by the US, the only change made by the US concerning the actionable subsidies is repeal of Step 2 program. Nevertheless, the terms of reference of a compliance panel is not limited to what the responding party claims to be the measures taken to comply. It is clear that the US shall take measures to withdraw all three subsidies or remove the adverse effects caused by these subsidies. In views of China, since the compliance panel is obliged to examine whether the measures taken by the US is consistent with the covered agreement, it is necessary for the panel to examine whether or not the remaining two programs (ML and CCP programs) are still causing serious prejudice.

3. CONCLUSIONS

17. To conclude, China requests the compliance panel to find that:

1) it is the set of provisos in the Agreement of Agriculture(especially the Articles 10.1 and 8) and SCM Agreement (particularly Articles 1, 3.1(a) and 3.2) *plus* item (j) in the Illustrative List that constitutes the complete basis for analyzing the nature of SGM 102 programs.

2) ML/CCP payment programs are within the scope of this compliance proceeding.

18. China reserves its right to address new arguments, and further develop the arguments set out herein, in its oral statement to the third party session of the first substantive meeting.

ANNEX A-8

THIRD PARTY SUBMISSION OF THE EUROPEAN COMMUNITIES

(5 January 2007)

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Australia – Automotive Leather	*Australia – Subsidies Provided to Producers and Exporters of Automotive Leather*, WT/DS126/R, adopted on 16 June 1999.
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Guatemala – Cement I	*Guatemala – Anti-Dumping Investigating Regarding Portland Cement from Mexico,* WT/DS60/AB/R, adopted on 25 November 1998.
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US – Shirts and Blouses	*United States – Measures Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, adopted on 23 May 1997.
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US-Zeroing	*United States – Laws, Regulations and Methodology for Calculating Dumping Margins ("Zeroing")*, WT/DS294/AB/R, adopted on 9 May 2006.

I. INTRODUCTION

1. The European Communities welcomes this opportunity to present its views on the legal claims by Brazil and the United States in relation to alleged non-compliance with the Dispute Settlement Body ("DSB") Recommendations and Rulings in "*United States – Subsidies on Upland Cotton*".

2. In the original panel proceedings the European Communities decided to intervene as a third party because of its systemic interest in the correct interpretation of the relevant WTO provisions, as well as in the correct application of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU"). At the DSB's meeting of 28 September 2006 the European Communities declared that it reserved its third-party rights in relation to the recourse to Article 21.5 of the *DSU* by Brazil.[1]

3. As a third party, the European Communities does not necessarily comment on every detail of the parties' submissions. The fact that the European Communities has not commented on a particular argument of the parties, or on the legal reasoning and findings in the Panel Report or Appellate Body Report should not be taken as an endorsement of such arguments, reasoning or findings. As is customary, the European Communities will refrain from analysing the facts of the case in detail but will present its views on a number of issues which raise systemic questions.

4. There are a number of systemic issues that arise from the parties' submissions and on which the European Communities wishes to comment. They will be dealt with under the following headings:

- Panel composition;
- Burden of proof;
- Adverse effects-related recommendations and rulings of the DSB:
  - Obligation to implement;
  - *Present* serious prejudice;
  - *Threat of* serious prejudice; and
- Mandatory/discretionary.

5. There are other issues, including the United States request for certain preliminary rulings, on which the European Communities intends to comment, and reserves its right to make further comments at the third party session of the Panel's first substantive meeting with the parties, once the parties' rebuttals are available.

II. PANEL COMPOSITION

A. INTRODUCTION

6. The European Communities would like to make a submission in relation to the statement made by Brazil at the meeting of the DSB on 26 October 2006, regarding the composition of the Panel established on 28 September 2006 pursuant to Article 21.5 of the *DSU* in this case.

7. Brazil had made a request under Article 8.7 of the *DSU* for the composition of a compliance panel. In its request, Brazil had asked the Director-General to nominate the three members of the panel in the original proceedings. Although all three members of the panel were available for service

[1] WTO Doc. WT/DSB/M/220 of 2 November 2006, paragraph 50.

in the Article 21.5 proceedings, the Director-General elected to call only one of the panellists back to service, and to nominate two new panellists.

8. In a letter to the Director-General following Brazil's request for composition under Article 8.7 of the *DSU*, the United States objected to the re-nomination of two of the original panellists, on the basis that they are nationals of third parties to the dispute. Brazil found the United States' objection "curious" and set out a number of reasons to justify its opinion in its statement on 26 October 2006.

B. RE-COMPOSITION OF PANEL NOT NECESSARY

9. Article 21.5 *DSU* states that:

> Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including *wherever possible* resort to the *original panel.* … (emphasis added)

10. A plain reading of the text of Article 21.5 *DSU* conveys the intention of the drafters of the *DSU* that if the original panel is available then it shall deal with the Article 21.5 *DSU* proceedings. If the original panel is available, it follows that there is no requirement for it to be re-composed, as it already exists and is available. It also follows that where the original panel is available, there is certainly no requirement for a new panel to be composed.

11. There are, however, certain limited circumstances in which the original panel would be unavailable. It would not be possible to refer the matter to the original panel if, for example, one of the panellists had resigned or died or was otherwise unavailable. It would also not be possible to refer the matter to the original panel if one of the panellists had a conflict of interest, for instance, if a panellist had acquired an equity stake in a United States or Brazilian cotton company. In such a case the panellist would be bound to resign and thus become unavailable. However, the European Communities is of the view that a panellist being a citizen of a third party to the dispute pursuant to an agreement already given under Article 8.3 of the *DSU* cannot for that reason alone require him to resign at the implementation stage. Where a panellist has the citizenship of a third party to the dispute then the presumption and starting point is that the parties should resort to the original panel.

12. If a panellist is unavailable the parties should apply Article 9.3 of the *DSU* by analogy so that "to the greatest extent possible the same persons shall serve as panellists". So the starting position should be that if one panellist is unavailable, then the other two panellists continue to serve on the panel.

C. CITIZENS OF THIRD PARTIES

13. Article 8.3 of the *DSU* states that:

> Citizens of Members whose governments[6] are parties to the dispute or third parties as defined in paragraph 2 of Article 10 shall not serve on a panel concerned with that dispute, unless the parties to the dispute agree otherwise.
>
> [6] In the case where customs unions or common markets are parties to a dispute, this provision applies to citizens of all member countries of the customs unions or the common markets.

14. The first clause of Article 8.3 of the *DSU* thus prohibits citizens of third parties from serving on "a panel concerned with that dispute". However, the second clause of Article 8.3 of the *DSU* permits the parties to agree that this prohibition does not apply.

15. The original panel had a Polish Chairman with Chilean and Australian (Mr. Daniel Moulis) Members.

16. Australia had reserved its third party rights when the original panel was established on 18 March 2003. It necessarily follows that Brazil and the United States must have (or must be deemed to have) entered into an unconditional agreement that the prohibition contained in the first clause of Article 8.3 did not apply to Mr. Moulis. Brazil and the United States thus agreed that Mr. Moulis was not to be prohibited from serving on "a panel concerned with that dispute", even though Australia was a third party. This must be so, otherwise the original panel (and presumably the original Panel Report) would be inconsistent with Article 8.3 of the *DSU*.

17. Both parties (the United States and Brazil) having entered into such an agreement that the prohibition in the first clause of Article 8.3 (precluding Mr. Moulis from serving on "a panel concerned with that dispute") was not applicable, there is no basis in the DSU for such agreement to be withdrawn at any time solely on the basis that Mr. Moulis is a national of a third party. The United States or Brazil or indeed both of them might subsequently have had "second thoughts", and might have wished Mr. Moulis to resign or to sack him. Perhaps as a result of a preliminary ruling; or after a hearing; or following questions; or following the issuance of the factual part or the interim report. But the DSU affords the parties no such right, and with good reason. It would obviously be deeply destructive to the independence of panellists, and intolerable from a systemic point of view, if either party could unilaterally sack a panellist, citing only as a reason that the panellist is a national of a third party, when agreement under Article 8.3 of the *DSU* has already been given.

18. The text of Article 8.3 *DSU* unequivocally supports the European Communities' interpretation on this matter. It states that "…third parties … shall not serve on <u>***a panel concerned with that dispute***</u>, unless the parties to *the dispute* agree otherwise." The use of the words "a panel concerned with that dispute" indicates that the drafters of this article intended that the rule in Article 8.3 (that is, both the prohibition and the agreement) are to apply more broadly than to their participation in the original proceedings ("the [original] dispute"). Article 21.5 *DSU* proceedings are certainly "concerned with" the original dispute. It therefore follows that the general prohibition on citizens of third parties serving as panellists applies in relation to their serving on panels considering Article 21.5 *DSU* proceedings; and the same must therefore be true of the agreement referred to in the second clause of Article 8.3 of the *DSU*.

19. Crucially, nothing in Article 8.3 *DSU* provides for a party to "the dispute" or "concerned with that dispute" to withdraw the consent ("agree[d] otherwise"), once given, for a citizen of a third party to serve on a panel concerned with that dispute. It is therefore not open to the United States to withdraw its consent in Article 21.5 *DSU* proceedings, in the same way as it would have been unable to withdraw its consent after the interim report was published or just before the final hearing of the original panel.

20. If a Member is free to object to the composition of a panel in such circumstances then there will be a strong perception amongst other Members that the Member has objected since it disagrees with the original panel's findings. This perception will be underlined by the fact that an objection was not made under Article 8.3 *DSU* in respect of the composition of the original panel.

D. ROLE OF ARTICLE 8.7 DSU

21. Article 8.7 of the *DSU* states that if the parties to the dispute cannot agree on the panellists the Director-General shall determine the panel's composition "in accordance with any relevant special or additional rules or procedures of the covered agreement or covered agreements which are at issue in the dispute". The European Communities submits that Article 21.5 of the *DSU* represents such a

relevant special rule. The Director-General, in exercising his discretion under Article 8.7 of the *DSU*, is therefore obliged to have regard to the provisions of Article 21.5 of the *DSU*.

22. Article 21.5 of the *DSU* states that an implementation "dispute shall be decided … wherever possible [by] resort to the original panel".

23. The European Communities agrees with Brazil that Article 21.5 *DSU* provides for resort to the original panel because the aim of Article 21.5 *DSU* proceedings is that they be dealt with as expeditiously as possible given that the dispute has already been settled by the panel (and in this case also by the Appellate Body).

24. The European Communities agrees with Brazil that "To facilitate the expeditious disposal of Article 21.5 proceedings, the provision calls for resort to the original panel in all but those narrow circumstances in which it is impossible for the original panellists to serve."[2] For the reasons set out above, in this particular case the United States should not have been able to successfully withdraw its agreement to an existing panellist continuing to serve on any panel concerned with the dispute solely on the grounds that he is a national of a third party.

25. It is the European Communities' view that in applying Article 8.7 of the *DSU*, in light of Article 21.5 of the *DSU*, the Director General was obliged to reject the United States attempt to withdraw its agreement under Article 8.3 of the *DSU* solely on the grounds that an existing panellist is a national of a third party.

E. UNATTRACTIVE PRECEDENT

26. The European Communities agrees with Brazil that the circumstances of this case set an unattractive precedent. The European Communities agrees with Brazil that this precedent could be invoked in other cases, because implementing Members could always object to the participation, in Article 21.5 *DSU* proceedings, of panellists who ruled against them in the original dispute.

F. PANEL SHOULD MAKE A FINDING OR RULING

27. The European Communities realises that it is not self-evident that this Panel should make findings or rulings regarding the propriety of its own composition. However, the European Communities believes that there is precedent for such a proposition, and that it is highly desirable in this case given the systemic importance of the issue.

28. The European Communities submits that the Panel has the authority to rule on the propriety of its own composition. Authority for this can be found in the *Australia – Automotive Leather* case. In that case the panel considered an Australian request that the panel terminate its work and, in effect, disestablish itself. In addition, the panel did not rule out the fact that, once the DSB has established a panel, the panel so established has the authority to rule on the propriety of its own establishment.[3]

29. Furthermore, the European Communities submits that, even if the parties do not address this issue directly in their submissions, the Panel has a duty to address it, as it is of fundamental importance for the correct interpretation of the *DSU* and for the smooth and equitable operation of

[2] Statement made by Brazil at the Meeting of the DSB on 26 October 2006.
[3] Panel Report, *Australia – Automotive Leather,* paragraphs 9.10 to 9.13.

the WTO dispute settlement system. In the *Mexico – HFCS (Article 21.5)* case the Appellate Body held that[4]:

> … panels have to address and dispose of certain issues of a fundamental nature, even if the parties to the dispute remain silent on those issues. In this regard, we have previously observed that "[t]he vesting of jurisdiction in a panel is a fundamental prerequisite for lawful panel proceedings."[34] For this reason, panels cannot simply ignore issues which go to the root of their jurisdiction – that is, to their authority to deal with and dispose of matters. Rather, panels must deal with such issues – if necessary, on their own motion – in order to satisfy themselves that they have authority to proceed.
>
> [34] Appellate Body Report, *United States – 1916 Act*, supra, footnote 32, para.54.

30. The European Communities submits that these cases provide authority for the view that the Panel should make findings on an analogous and very important systemic issue in the interpretation of the *DSU*. Indeed, the European Communities submits that it is vitally important that the Panel delivers a finding or ruling on this systemic issue to avoid the perception that Members can always object to the participation, in Article 21.5 *DSU* proceedings, of panellists who ruled against them in the original dispute.

III. BURDEN OF PROOF

31. The European Communities submits that Brazil, as the applicant in these Article 21.5 *DSU* proceedings, bears the burden of proving its assertions that the United States has failed to implement, in a timely and complete manner, the recommendations and rulings of the DSB.

32. The general principles applicable to burden of proof, as stated by the Appellate Body in *US – Shirts and Blouses*, require that a party claiming a violation of a provision of the WTO Agreement by another Member must assert and prove its claim.[5] In the present Article 21.5 *DSU* proceedings the European Communities submits that it is Brazil, which has challenged the United States' implementation of the recommendations and rulings of the DSB, that bears the burden of proving that the United States has not implemented them in a timely and complete manner. It is therefore the responsibility of Brazil to submit evidence sufficient to establish a *prima facie* case that the United States has not implemented the recommendations and rulings of the DSB in a timely or complete manner. Once Brazil has done so, it is for the United States to submit evidence sufficient to rebut that *prima facie* case.

33. The European Communities also recalls that the Appellate Body has observed that various international tribunals, including the International Court of Justice, have generally and consistently accepted that the party that asserts a fact, whether claimant or respondent, is responsible for providing proof thereof.[6]

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[4] Appellate Body Report, *Mexico – HFCS (Article 21.5)*, paragraph 36.
[5] Appellate Body Report, *US – Shirts and Blouses*, pages 14 to 16.
[6] Appellate Body Report, *US – Shirts and Blouses*, page 14.

IV. ADVERSE EFFECTS-RELATED RECOMMENDATIONS AND RULINGS OF THE DSB

A. OBLIGATION TO IMPLEMENT

34. Brazil claims that between the expiry of the implementation period on 21 September 2005 and the elimination of Step 2 payments on 1 August 2006, there did not "exist" any United States "measures taken to comply" with the adverse effects-related recommendations and rulings of the DSB.[7]

35. In the view of the European Communities, one of the tasks incumbent on the present Article 21.5 *DSU* Panel is to examine whether by taking no positive action the United States could nevertheless be "in conformity with" its obligations under the *SCM Agreement*. As the Appellate Body in *Canada – Aircraft (Article 21.5)* held:

> Proceedings under Article 21.5 do not concern just *any* measure of a Member of the WTO; rather, Article 21.5 proceedings are limited to those "measures *taken to comply with* the recommendations and rulings" of the DSB. In our view, the phrase "measures taken to comply" refers to measures which have been, or which should be, adopted by a Member to bring about compliance with the recommendations and rulings of the DSB. In principle, a measure which has been "taken to comply with the recommendations and rulings" of the DSB, will *not* be the same measure as the measure which was the subject of the original dispute, so that, in principle, there would be two separate and distinct measures: the original measure which *gave rise* to the original recommendations and rulings of the DSB, and the "measures taken to comply" which are – or should be – adopted to *implement* those recommendations and rulings.[8]

36. However, from the text of Article 7.8 of the *SCM Agreement* it is not clear that the United States even had to actually *do* anything to comply with the findings and recommendations of the original panel.

37. Article 7.8 of the *SCM Agreement* states that:

> Where a panel report or an Appellate Body report is adopted in which it is determined that any subsidy has resulted in adverse effects to the interests of another Member within the meaning of Article 5, the Member granting or maintaining such subsidy shall <u>*take appropriate steps*</u> *to remove the adverse effects*[9] or shall withdraw the subsidy.

38. Thus, the text of Article 7.8 of the *SCM Agreement* does not state expressly that a Member that has been requested by the DSB to implement its recommendations and rulings under Article 7.8 of the *SCM Agreement* actually has to *do* anything. Article 7.8 of the *SCM Agreement* gives the implementing Member two choices as to how to implement DSB recommendations and rulings. It can "take appropriate steps to remove the adverse effects [of the subsidy]". On the other hand, an implementing Member also has the choice to comply with the DSB's recommendations and rulings by "withdraw[ing] the subsidy".

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[7] Section 6 of Brazil's First Written Submission.
[8] Appellate Body Report, *Canada – Aircraft (Article 21.5)*, paragraph 36.
[9] European Communities' emphasis added.

39. It is clear that between the implementation date of 21 September 2005 and 31 July 2006 the United States did not withdraw any of the subsidies in question. However, this does not automatically mean that the United States has not complied with the DSB's recommendations and rulings as it was open for the United States to choose instead to "take appropriate steps to remove the adverse effects".

40. The European Communities submits that in "tak[ing] appropriate steps to remove the adverse effects" an implementing Member can exercise its discretion as to how best to remove those adverse effects. It could choose to do so by enacting new legislation, amending current legislation, or by an executive order or other types of administrative action. These are all examples of positive acts which could be taken by an implementing Member.

41. However, the European Communities further submits that "tak[ing] appropriate steps" may also include, in certain cases, taking no positive action at all; in other words, doing nothing. The test which taking no positive action has to meet in order to comply with the *SCM Agreement* is that it constitutes "appropriate steps to remove the adverse effects". The question as to whether taking no positive action actually is "appropriate" and actually does "remove" the adverse effects should be judged by a careful analysis of the particular facts and circumstances of each case. It may be in certain cases that other facts and circumstances have changed to such an extent that the adverse effects of the subsidies have stopped; for instance, a subsidy may have expired and adverse effects may have stopped.

42. If there are three subsidies at issue and the original panel holds that they cumulatively had an adverse effect, it is possible that the removal of one of those subsidies could remove the adverse effect.

43. In a case where the subsidy or adverse effects are discontinued the European Communities submits that the complaining party in Article 21.5 *DSU* proceedings is bound to analyse whether the implementing party has taken appropriate steps to remove the adverse effects with reference to "present" circumstances rather than the possibly rather different circumstances which may have existed when the DSB made its original rulings and recommendations. However, analysis of the "present" circumstances and context will invariably entail analysis of the latest relevant statistical and financial information and reports, so in this sense the analysis cannot be absolutely contemporaneous with the position on the ground. However, the complaining party in Article 21.5 *DSU* proceedings should ensure that its analysis is as up to date as is possible and the European Communities would expect that the Panel will employ a "reasonableness" test in its analysis thereof.

44. In the *US – Softwood Lumber VI, (Article 21.5)* panel report it was noted that,

> [t]he role of a panel in an Article 21.5 panel proceeding is to evaluate the challenged measure to determine its consistency with the defending Member's obligations under the relevant WTO Agreements.[10]

45. Thus, it said, the panel,

> is not limited by its original analysis and decision – rather, it is to consider, with a fresh eye, the new determination before it, and evaluate it in light of the claims and arguments of the parties in the Article 21.5 proceeding.[11]

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[10] Panel Report, *US – Softwood Lumber VI (Article 21.5)*, paragraph 7.12.
[11] Panel Report, *US – Softwood Lumber VI (Article 21.5)*, paragraph 7.12.

46. The European Communities submits that the panel's reasoning in *US – Softwood Lumber VI (Article 21.5)* on this point should apply in the present case. Although the United States may not have taken any positive action to comply with the panel and Appellate Body's findings and recommendations between the implementation date of 21 September 2005 and 31 July 2006, the Panel cannot, subject to the principle of *res judicata*, be limited by the earlier panel and Appellate Body reports as it must make a new determination in the present Article 21.5 *DSU* proceedings.

47. In *US – Softwood Lumber VI (Article 21.5)*, the panel also observed that,

> [w]hile we cannot preclude the possibility that a Member might implement a DSB recommendation by specifically answering points raised by a panel (or the Appellate Body) in the relevant decisions, this is by no means required by the DSU.[12]

48. On appeal the Appellate Body concluded that the panel's statements in this regard did not violate Article 11 of the *DSU*. Again, this case demonstrates that the lack of positive action taken by the United States to comply with the panel and Appellate Body's findings and recommendations between the implementation date of 21 September 2005 and 31 July 2006 is not necessarily fatal to its defence. As stated above, subject to the principle of *res judicata*, the Panel cannot be restricted by the earlier panel and Appellate Body reports as it must make a new determination in the present Article 21.5 *DSU* proceedings.

B. PRESENT SERIOUS PREJUDICE

49. In its adverse effects-related recommendations and rulings, the original panel, as affirmed by the Appellate Body, found that the price-contingent United States marketing loan program, counter-cyclical payment program and Step 2 program of the FSRI Act of 2002 caused significant price suppression in the world market for upland cotton, in violation of Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement.* The panel found that:

> the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice findings.[13]

50. The DSB adopted the panel and Appellate Body reports that obliged the United States to remove the adverse effects caused by the subsidies, or to withdraw the subsidies by 21 September 2005.

51. In the present Article 21.5 *DSU* proceedings Brazil claims that the United States did not repeal or amend any of the three price-contingent subsidy programs until 1 August 2006, when it finally discontinued solely the Step 2 program. Brazil claims that the far larger marketing loan and counter-cyclical payment programs have not been removed or amended.

52. In the second of Brazil's claims concerning adverse effects-related recommendations and rulings of the DSB, Brazil claims that the non-repealed price-contingent United States marketing loan and counter-cyclical payment programs under the FSRI Act of 2002 cause *present*[14] serious prejudice in the form of significant price suppression in the world market for upland cotton, and an increase in the world market share, in violation of Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*. In other words, Brazil claims that, to the extent measures taken to comply with the adverse-effects related recommendations and rulings of the DSB exist (i.e., the repeal of Step 2 and the non-repeal of

[12] Panel Report, *US – Softwood Lumber VI (Article 21.5)*, paragraph 7.12.
[13] Panel Report, *US – Upland Cotton,* paragraph 7.1501.
[14] European Communities' emphasis added.

the marketing loan and counter-cyclical payment programs), those measures are deficient, and result in inconsistencies with the covered agreements, within the meaning of Article 21.5 of the *DSU*.

53. With the exception of those circumstances set out in Part IV.C of this submission of the European Communities, in order for Brazil to be able to make a successful claim that the price-contingent United States marketing loan and counter-cyclical payment programs have caused it serious prejudice, it must be able to evidence that the serious prejudice is actually *present*.

54. In establishing its claim, Brazil relies on data covering the marketing year 2005 – as well as additional available data since marketing year 2002, the first marketing year under the FSRI Act of 2002.[15] Brazil states in its first written submission that in order to establish "present" serious prejudice the complaining party must use data from the most recently completed marketing year.[16] However, the European Communities submits that, in establishing a claim of *present* serious prejudice, Members are obliged to rely on the most recent <u>relevant</u> data <u>reasonably available</u> to them. For instance, the first quarter of the United States' marketing year 2006 for upland cotton runs from 1 August 2006 until 31 October 2006. It is the European Communities' view that, if the data for the first quarter of marketing year 2006 was relevant and reasonably available to Brazil, it would have been obliged to establish any claim of *present* serious prejudice with reference to that data in its first written submission on 17 November 2006, a date which is almost three weeks after the end of the first quarter of marketing year 2006.

55. The United States, as the defending party in this dispute, is also obliged to respond to any complaint of *present* serious prejudice with reference to the most recent reasonably available relevant data. Even if the data for the first quarter of marketing year 2006 had not been reasonably available to Brazil, but it became reasonably available to the United States in the period between the lodging of Brazil's first written submission and the lodging of the United States' first written submission, the United States would be obliged to refer to it in responding to a complaint of *present* serious prejudice. The first written submission of a defending party in a matter brought under the *DSU* is not a rebuttal, so the defending party is obliged to set out its arguments and, in responding to any complaint of *present* serious prejudice, to refer to the most recent reasonably available and relevant data notwithstanding the data which the complaining party has referred to.

56. Support for the European Communities' approach can be seen in the panel's and Appellate Body's approach to the analogous concept of "present injury" in anti-dumping cases. For instance, in *US – Softwood Lumber VI* the panel stated that it must be clear from an authority's determination of threat of material injury that the authority has evaluated "how the future will be different from the <u>immediate</u> past, such that the situation of no present material injury will change in the imminent future to a situation of material injury . . . .".[17] This also applies to considerations of present injury. As the panel stated in *Mexico – Rice AD Measures*:

> An authority that fails to examine data that includes the most recent available information will not be in a position to make judgments about the immediate past. The same can be said about findings of present injury. An authority can only make

[15] The United States' marketing year for upland cotton runs from 1 August to 31 July. The 2005 marketing year covered the period from 1 August 2005 until 31 July 2006.

[16] Paragraph 212 of Brazil's First Written Submission.

[17] Panel Report, *US – Softwood Lumber VI*, paragraph 7.58.

> objective determinations about the present, or the imminent future, if it is examining a period that <u>includes</u> the most recent available information.[18]

57. The European Communities submits that the Panel can apply the above reasoning in relation to "present injury" in anti-dumping cases to the interpretation of "present serious prejudice" in subsidies cases such as the present case. The two concepts are very similar and have similar objects and effects within their respective agreements which are annexed to the WTO Agreement. Indeed, while Article 3.1 of the *Anti-Dumping Agreement* and Article 15.1 of the *SCM Agreement* require that a determination of injury be based on "positive evidence", Article 6.8 of the *SCM Agreement* states that the existence of serious prejudice should be determined "on the basis of the information submitted to or obtained by the panel". The Appellate Body has confirmed that the reference to "positive evidence" within the meaning of Article 3.1 of the *Anti-Dumping Agreement* necessitates a "sufficiently relevant nexus between the data relating to the period of investigation and current injury".[19] Similarly, the existence of "present serious prejudice" can only be properly determined if such a sufficiently relevant nexus exits between data submitted to or obtained by the Panel and present serious prejudice.

58. The European Communities would submit that the more recent the data, the more convincing will be the demonstration of *present* serious prejudice. For instance, if the most recently completed marketing year for which figures are available is from ten years ago then the European Communities would submit that this would clearly be unreasonably old data to be used in calculating whether a measure constituted "present" serious prejudice. In the majority of cases involving a "marketing year" the European Communities would expect that the "most recently completed marketing year" would be interpreted by a panel as meaning the data for the marketing year directly preceding the current marketing year, or the data for the quarterly or six monthly periods in the current marketing year. Only in very special cases should the Panel consider making an exception to this general principle.

C. THREAT OF SERIOUS PREJUDICE

59. In section 8 of Brazil's first written submission, Brazil seems to evidence the *threat* of serious prejudice on the basis of "projections" of the United States' subsidy outlays going forward.

60. The European Communities recalls the findings by the original panel with respect to Brazil's claims of the *threat* of serious prejudice in those proceedings. In contrasting "*threat* of serious prejudice" with "*present* serious prejudice," the original panel found as follows:

> We believe that "threat" of serious prejudice refers to something distinct from serious prejudice. However, in terms of the rising continuum of seriously prejudicing another Member's interests, that ascends from a "threat" of serious prejudice up to "serious prejudice," we see "serious prejudice" as necessarily *including* the concept of a "threat" and *exceeding* the presence of a "threat" for purposes of answering the relevant inquiry. This is confirmed by the text of footnote 13 of the *SCM Agreement*, which indicates that serious prejudice "includes" threat of serious prejudice.[20]

61. In this respect, the European Communities concurs with Brazil's statement in its first written submission in this case that present serious prejudice would normally be *preceded in time* by a

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[18] Panel Report, *US - Rice AD Measures*, paragraph 4.410. See also: Appellate Body Report, *US - Rice AD Measures*, paragraph 167.

[19] Appellate Body Report, *US - Rice AD Measures*, paragraph 167.

[20] Panel Report, *US – Upland Cotton*, paragraph 7.1495.

prejudice that threatens to become serious, and serious prejudice would be the realisation of a threat of serious prejudice.

62. The text of the cited legal provisions leads the European Communities to conclude that either serious prejudice, or threat of serious prejudice, or both in combination, may trigger the remedies available in Article 7 of the *SCM Agreement*. The existence of either one, or the other, is both a necessary and sufficient condition, in and of itself, to achieve this.[21]

63. The European Communities agrees with the original panel's conclusion that a finding of present serious prejudice includes the concept of threat of serious prejudice. The European Communities also agrees with the original panel's conclusion that a finding of present serious prejudice is a sufficient condition to trigger the remedy available in Article 7.8 of the *SCM Agreement*.

V. ALLEGED SO-CALLED "MANDATORY-DISCRETIONARY" DISTINCTION

64. The United States submits that, since Brazil is making an "as such" claim against the US marketing loan and counter-cyclical payment "programs", in order to succeed, Brazil must "show" that the measure "mandates" a breach of Articles 5(c) and 6.3(c) or 6.3(d) of the *SCM Agreement*. The United States does not refer to any provision of WTO law to support its submission. Rather, the United States asserts that such a requirement "has been consistently applied in GATT and WTO dispute settlement proceedings". The United States submits that the panel in the original dispute appeared to confuse the "mandatory-discretionary" distinction with the different question of whether something can be challenged as a measure if it has no binding legal effect. The United States further submits "more specifically" that Brazil would have to demonstrate that the measure mandates actions "that will necessarily cause the kind of effects alleged by Brazil under Article 6.3(c) and 6.3(d) of the *SCM Agreement*." According to the United States, the provision in question "simply sets out the conditions" under which payment will be made, and for that reason does not "mandate" anything; and thus cannot be WTO inconsistent.[22]

65. The European Communities disagrees with the United States submissions. The European Communities considers that no such requirement can be derived from the text of the *SCM Agreement* or any other WTO agreement, nor from the case law. The European Communities observes that the United States does not actually explain what, according to the United States, the content of the distinction is supposed to be. Evidently, it is not and cannot be co-extensive with the question of causation. Nor can it be that a measure is automatically WTO consistent merely because it contains conditions. Contrary to what the United States submits, this matter was litigated at length before the Appellate Body in *US-Zeroing*, and the arguments of the United States were not accepted.

66. Referring to and summarising its submission in that case, the European Communities recalls that the legal basis for, origins, evolution and content of the so-called mandatory/discretionary doctrine are obscure. The United States cites no legal basis for the alleged rule in the WTO Agreements. A careful review of past GATT and WTO panel reports reveals that under the heading "mandatory/discretionary" one will not in fact find a homogenous, systematic and consistent articulation of the same point or principle. Rather, one finds slightly different ideas or concepts,

[21] Panel Report, *US – Upland Cotton*, paragraphs 7.1495 to 7.1497.
[22] United States first written submission, paragraphs 196 to 202.

applied to disparate factual situations, and often leading to rather different results.[23] The mandatory/discretionary rule is not anywhere articulated in the WTO agreements, and certainly not in the general, abstract and mechanistic terms in which it is invoked by the United States. Rather, its alleged existence is entirely based on the alleged "consistent practice" of past GATT and WTO panels. But there is no such "consistent practice".

67. One-by-one, some of the things that it has from time-to-time been suggested the so-called mandatory/discretionary rule might stand for have, particularly on review by the Appellate Body, fallen by the way-side. There is, for example, no need that the measure be adopted by the "legislature" as opposed to the "executive". Any measure imputable to a Member is susceptible to review.[24] There is, for example, no need that the measure is "binding" in municipal law. Even "non-binding" measures are susceptible to review.[25] It is irrelevant, for example, if the measure can be changed, or how it might be changed.[26] A measure may be inconsistent even if it has not yet been applied (although evidence of its "as applied" use may evidence a finding of inconsistency).[27] Also irrelevant is the assertion that the municipal law measure is allegedly susceptible to various interpretations by the municipal courts.[28]

68. The United States has in the past asserted that the "mandatory/discretionary" rule means that the measure must *in all cases* require WTO-inconsistent action before it can be impugned. The European Communities does not agree that such a rule exists or is to be mechanistically applied. With the possible exception in practice of numbers, it is <u>never possible</u> to say that two general and normative rules not expressed in identical terms will *always* produce the same result when applied to any set of facts. It is always possible to imagine a set of facts to which the application of the two rules will produce different results. This simply results from the fact that there is a penumbra associated with all language, especially when used in relatively abstract terms. The *mechanistic* application of an "in all cases" test thus stands for the proposition that general municipal measures should never or almost never be found "as such" inconsistent; a proposition that flatly contradicts the provisions of the *SCM Agreement* and the *WTO Agreement*. In the light of Article XVI:4 of the WTO Agreement and Article 32.5 of the *SCM Agreement*, Members must ensure conformity with WTO law, either through direct effect, or through implementing measures that are themselves in conformity with WTO law.

69. The European Communities believes that, just as the "mandatory/discretionary" rule is not, in truth, borne of any abstract basic principle expressed in the WTO agreement or elsewhere, but has rather been puffed-up by dubious assertion based on specific past cases; so we may expect, quite appropriately, to witness its demise, on a case-by-case basis. The Appellate Body could confirm,

[23] See, for example, *Mandatory and Discretionary Legislation: the Continued Relevance of the Distinction under the WTO*, Sharif Bhuiyan, Journal of International Economic Law 5(3), 571-604; and *The Mandatory/Discretionary Doctrine in WTO Law, The US-Section 301 Case and its Aftermath*, Yoshiko Naiki, Journal of International Economic Law 7(1), 23-72.

[24] Such a requirement was sometimes alleged based on the wording of a GATT Working Party Report commenting on the GATT Protocol of Provisional Application, suggesting that a "mandatory" measure "imposes on the ***executive*** authority requirements which cannot be modified by ***executive*** action". Such an assertion does not hold good under WTO law (Appellate Body Report, *US-Corrosion-Resistant Steel*, paragraph 81).

[25] Appellate Body Report, *US-Corrosion-Resistant Steel*, paragraph 38 (US "non-binding" argument) and paragraph 85; Appellate Body Report, *Guatemala – Cement I*, paragraph 69, footnote 47. The US now agrees with the EC and the Appellate Body on this point (US first written submission, footnote 286).

[26] Appellate Body Report, *US-Corrosion-Resistant Steel*, paragraph 39 (US "modification" argument) and paragraphs 81 to 101.

[27] Appellate Body Report, *US-Corrosion-Resistant Steel*, paragraph 82.

[28] Appellate Body Report, *US-1916 Act*, paragraph 90.

once and for all, that there is, in truth, no such principle. In the opinion of the European Communities, that is what it has effectively done by finding that such a "rule" is not to be mechanistically applied. Alternatively, the Appellate Body may, in one successive case after another, explain why the rule does not avert an "as such" finding of inconsistency in the particular case. Whether it's a quick execution or a slow and painful death, the end result is the same. This view is confirmed by the Appellate Body Report in *US-Zeroing*.[29]

[29] Appellate Body Report, *US-Zeroing*, paragraphs 62 and 208 (summarising US argument); paragraphs 67, 68 and 210 (summarising EC argument) and paragraphs 211 to 214 (Appellate Body findings).

ANNEX A-9

THIRD PARTY SUBMISSION OF JAPAN

(5 January 2007)

TABLE OF CONTENTS

I. INTRODUCTION

1. Japan welcomes the opportunity to present its views to the Compliance Panel in this dispute, which was brought by Brazil to challenge the implementation by the United States of the recommendations and rulings of the Dispute Settlement Body (DSB) in *United States – Subsidies on Upland Cotton* (*Upland Cotton*).

2. As a third party, Japan's comments stem from its systemic interest in ensuring objective and consistent interpretation of the WTO agreements, in particular the Agreement on Subsidies and Countervailing Measures (ASCM) and the Dispute Settlement Understanding (DSU). Japan would like to address the following issues discussed in the First Written Submissions of Brazil and the United States:

- The standards discussed by Brazil for establishing "threat of serious prejudice" under Part III of the ASCM;
- The U.S. argument that the Panel lacks the authority to issue a ruling where a party has taken no action to bring a measure into compliance; and
- The importance of ensuring that, when a Member resorts to an outside source or index, it fully explains its rationale for doing so.

II. ARGUMENT

A. THE THREAT OF SERIOUS PREJUDICE STANDARDS DISCUSSED BY BRAZIL ARE FLAWED

3. Japan is of the view that the most important issue of general interest raised in this dispute is the appropriate standard for establishing threat of serious prejudice under Part III of the ASCM.[1] As at least one panel has recognized, neither Article 5(c) nor footnote 13 of the ASCM "defines or elaborates" on the concept of "serious prejudice" to the interests of another Member, much less the concept of "threat".[2] Reflecting the lack of textual guidance, Brazil discusses two markedly different standards for adoption by the Panel. First, Brazil presents for adoption a standard of "'significant likelihood' of serious prejudice in the future".[3] Second, based on the United States position in the original proceeding, Brazil ascribes to the United States a standard based on Article 15.7 of the ASCM.[4] As explained below, in Japan's view, each proposal has attributes, but ultimately both are flawed and should be rejected.

4. This issue is exceedingly important and has far-reaching implications. Japan asks the Panel to scrutinize the two proposals, taking into consideration the comments set forth below.

[1] *See* Agreement on Subsidies and Countervailing Measures, Art. 5(c) and n.13.
[2] *Korea – Measures Affecting Trade in Commercial Vessels*, WT/DS273/R (7 March 2005), para. 7.529.
[3] *United States – Subsidies on Upland Cotton*; *Recourse by Brazil to Article 21.5 of the DSU,* WT/DS267, Brazil's First Submission, para. 259.
[4] *Id*. at paras. 254 – 258. *See* ASCM, Article 15.7.

1. The Proposal Brazil Ascribes to the United States is Flawed – The Threat Standard of Part V of the Agreement on Subsidies and Countervailing Measures Should Not Be Imported to Part III

5. The standard Brazil ascribes to the United States is drawn from Article 15.7 of the ASCM. The standard has two-parts as follows:

1. The "change in circumstances which would create a situation in which the subsidy would cause [serious prejudice] must be clearly foreseen and imminent"; and

2. The threat determination "shall be based on facts and not merely on allegation, conjecture or remote possibility".[5]

In essence, this proposal would import the threat of material injury standard from Part V to Part III of the ASCM for the purposes of determining "threat of serious prejudice".

6. As discussed in Section II.B.2. below, Japan agrees that an evidentiary requirement is an important part of a threat standard. However, as explained below, Japan would reject this legal standard.

7. Brazil, in its First Submission, demonstrates that textual reasons[6] and practical reasons[7] militate against adopting the "clearly foreseen and imminent" legal standard. For the sake of brevity, Japan will not repeat them.

8. There is another important reason to reject this proposal. Parts III and V of the ASCM serve markedly different purposes. The Part V legal standard for "threat" reflects this difference and, therefore, is an inappropriate standard for "threat of serious prejudice" under Part III. Part V addresses countervailing measures. It cabins the discretion granted to national authorities to conduct investigations and impose countervailing duties (CVDs). Article 15 of Part V sets out requirements for injury determinations by national authorities. Article 15.7, inter alia, establishes a rigorous two-part standard that must be met before a CVD can be applied on the basis of an alleged "threat" of material injury. One part of the standard is an evidentiary requirement ensuring that a finding of "threat" is based on facts.[8] The other part is a strict legal standard stating the conditions that must be met before an affirmative finding of "threat" can be made.[9]

9. As compared to the concept of actual "injury", the concept of "threat of material injury" by nature is less defined. Indeed, in the anti-dumping context, the Appellate Body has referred to "threat" findings as involving "intrinsic uncertainty".[10] In Part V of the ASCM, Articles 15.7 and 15.8 address this difference. Along with the exhortation of Article 15.8 that national authorities exercise "special care" in threat cases, the two parts of the Article 15.7 standard work together to limit the discretion of national authorities and guarantee against misuse.[11]

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[5] *Id.*

[6] *Id.*, para. 255.

[7] *Id*., para. 256.

[8] *See* ASCM, Article 15.7, first sentence.

[9] *Id.*, second sentence.

[10] *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States; Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW (22 October 2001), para. 85.

[11] *See, e.g., United States – Investigation of the International Trade Commission in Softwood Lumber from Canada; Recourse to Article 21.5 of the DSU by Canada*, WT/DS277/AB/RW (13 April 2006), para. 96 (Article 15.7 of the ASCM "enjoin[s] a panel to *scrutinize carefully* the inferences and explanations of the

10. The original Panel in this proceeding properly recognized that ASCM Part V, for a variety of reasons, may not be proper context for interpreting and applying Part III.[12] The Panel recognized the significant differences in the purposes and instruments of Part III, which addresses WTO claims of "serious prejudice", and Part V, which addresses national authorities' conduct of CVD investigations and imposition of CVDs, even though both Part III and Part V address subsidies.

11. In this specific case, Part III issues are completely devoid of concerns relating to limiting the discretion of national authorities to prevent misuse thereof in the conduct of domestic CVD investigations set forth above that apply to Part V. In a "threat of serious prejudice" claim under Part III, the provisions and standards are applied by panels and the AB. No national authority is involved.

12. The Panel should reject the standard Brazil ascribes to the United States for this reason, as well as those set out by Brazil in paragraphs 255-256 of its First Submission relating to textual analysis of ASCM Article 5(c), accompanying note 13 and Article 15.7 and to the possible effect of precluding remedies for certain types of subsidy programs.

2. Brazil's Proposed Standard Does Not Explicitly Include an Evidentiary Requirement

13. Brazil proposes a separate, less stringent standard for establishing "threat of serious prejudice". Brazil proposes that the Panel find that a "threat of serious prejudice" exists where there is a "'significant likelihood' of serious prejudice in the future."13 As an initial matter, Japan notes that this proposal is incomplete as it does not include an explicit evidentiary requirement.[14] An explicit evidentiary requirement such as that set forth in the first sentence of ASCM Article 15.7[15] is a crucial component of any "threat" standard. It is necessary to tie to real world facts what otherwise is an amorphous concept.

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investigating authority in order to ensure that any projections or assumptions made by it, as to likely future occurrences, are adequately explained and supported by positive evidence on the record" (emphasis added; referring also to Article 3.7 of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (AD Agreement)) citing *United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia*, WT/DS177, 178/AB/R (1 May 2001), para. 136; *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States; Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW (22 October 2001), para. 85.

Panels have rigorously applied the standard governing "threat" in the safeguard context under Articles 4.1(b) and 4.2(a) of the Agreement on Safeguards and in the anti-dumping context under Article 3.7 of the AD Agreement. *See, e.g., Argentina – Definitive Safeguard Measure on Imports of Preserved Peaches*, WT/DS238/R (14 February 2003), paras. 7.83 – 7.133 (rejecting affirmative threat finding of national authority); *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products*, WT/DS207/R (3 May 2002), paras. 7.163 – 7.174 (same); *Argentina – Safeguard Measures on Imports of Footwear*, WT/DS121/R (25 June 1999), paras. 8.281 – 8.286 (same); *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States; Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW (22 October 2001), paras. 76 – 101 (upholding Panel's rejection of national authority's affirmative threat finding).

[12] *See, e.g., United States – Subsidies on Upland Cotton*, WT/DS267/R (8 September 2004), para. 7.1167.

[13] Brazil's First Submission, para. 259.

[14] Japan notes, however, that, after setting out the proposed standard, Brazil lists a number of factors for consideration, which indicates an appreciation of the evidentiary concerns raised by the amorphous nature of threat claims. *See id*., para. 260.

[15] *See also* Agreement on Safeguards, Article 4.1(b) ("A determination of the existence of a threat of serious injury shall be based on facts and not merely on allegation, conjecture or remote possibility"); AD Agreement, Article 3.7 ("A determination of a threat of material injury shall be based on facts and not merely on allegation, conjecture or remote possibility").

14. Japan recognizes that this position could be criticized as inappropriately importing a provision from Part V, contrary to (or inconsistent with) Japan's argument in Section II.A.1. above. However, in this instance, the importation makes sense. Any type of threat determination – whether it be of serious prejudice, material injury or serious injury – must be grounded in fact.

15. Turning to Brazil's proposed legal standard – "significant likelihood" – Japan is of the view that the standard is more balanced than the legal standard of Article 15.7 of the ASCM. However, Brazil's proposed standard offers little concrete guidance – what, exactly, constitutes a significant likelihood? Japan notes that panels previously have had occasion to discuss "likely" and "likelihood". In a proceeding involving the AD Agreement, the panel examined the meaning of "likely" as it is used in Article 11.2 in the phrase "whether the injury would be likely to continue or recur".[16] In a later proceeding, a panel examining a threat determination under Article 4.1(b) of the Agreement on Safeguards examined the phrase "clearly imminent", concluding that it signaled that an affirmative threat finding required the existence of a "high degree of likelihood that the anticipated serious injury will materialize in the very near future."[17] The inclusion of the word "significant" suggests a stricter standard than that examined by the panel in *U.S. – DRAMS* and comes closer to a "high degree of likelihood" as discussed in *Preserved Peaches*, but the question remains as to what exactly would constitute a "significant likelihood". In any case, these earlier panel reports might be of assistance in evaluating Brazil's proposal.

3. Final Comments on Threat of Serious Prejudice

16. When the Panel addresses the issue of the appropriate standard for "threat of serious prejudice", Japan understands it will proceed in accordance with Article 3.2 of the DSU and Section 3 of the Vienna Convention on the Law of Treaties.

17. In addition, Japan asks the Panel to consider that the "threat" standard must be applicable to circumstances that are very different from those in this case. As Brazil notes, the standard must not, by its very structure, ignore an entire class of threat cases, especially cases in which serious prejudice had been established in an earlier proceeding.[18] At the same time, though, the standard must be strict enough to discourage specious threat claims.

B. The U.S. Argument that the Panel Lacks the Authority to Issue a Ruling Where a Party Has Taken No Action to Bring a Measure Into Compliance is Flawed and Should be Rejected

18. The United States argues that the Panel lacks the authority to address Brazil's arguments regarding the U.S. Marketing Loan Program and Countercyclical Program.[19] Under scrutiny, the U.S. argument reduces to a position that is indefensible – the U.S. would subject to Article 21.5 review a Member that in good faith attempts to alter a non-compliant measure to bring it into compliance, but would insulate from Article 21.5 review a Member that takes no action to bring a non-compliant measure into conformity with WTO provisions.

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[16] *See United States – Anti-Dumping Duty on Dynamic Random Access Memory Semiconductors (DRAMS) of One Megabit or Above from Korea*, WT/DS99/R (29 January 1999), paras. 6.44-6.51.

[17] *Argentina – Definitive Safeguard Measure on Imports of Preserved Peaches*, WT/DS238/R (14 February 2003), para. 7.120.

[18] *Cf*. Brazil's First Submission, paras. 256-258.

[19] *See* U.S. First Submission, paras. 45 – 48; *see also id*., paras. 49 – 56.

19. The United States cites the Appellate Body report in EC – Bed Linen 21.5 to support its position[20], but the citation is unavailing. The U.S. characterization of the Appellate Body report is questionable. The most pertinent part of the report is the following statement:

> 87. We conclude, therefore, that, in these Article 21.5 proceedings, India has raised the *same* claim under Article 3.5 relating to "other factors" as it did in the original proceedings. In doing so, India seeks to challenge an aspect of the original measure which has not changed, *and which the European Communities did not have to change*, in order to comply with the DSB recommendations and rulings to make that measure consistent with the European Communities' WTO obligations.[21]

Thus, the situation in *EC – Bed Linens 21.5* is not analogous to the instant proceeding.

20. The U.S. argument, if accepted, could create an endless loop of litigation where a Member refused to alter a measure found to be non-compliant. By cutting off access to review under Article 21.5, the U.S. argument would require the Member that won the original challenge to bring a separate dispute regarding the unchanged measure. In Japan's view, this result is to be avoided.

21. Japan asks the Panel to reject this U.S. argument.

C. CONCERNS RAISED BY THE PARTIES' USE OF OUTSIDE SOURCES

22. In a case as complex as *Upland Cotton*, the parties of necessity resort to non-WTO related sources to advance their positions. To ensure that each outside source is properly used, panels and the Appellate Body should scrutinize each source and its relationship to the proposition it is alleged to support.

23. This proceeding presents many examples of this practice. Japan wishes to focus on two in particular – Brazil's reliance on the OECD Arrangement on Officially Supported Export Credits (OECD Arrangement)[22] and the U.S. use of a report by the International Cotton Advisory Committee (ICAC).[23]

1. Brazil's Use of the OECD Arrangement on Officially Supported Export Credits

24. Brazil relies on the OECD Arrangement for the limited purpose of establishing that fees for Export Credit Guarantees (ECGs) under the U.S. General Sales Manager (GSM) 102 program are less than the minimum premium rates (MPRs) in the Arrangement (and, to simplify Brazil's argument, are thus below market).[24]

25. In Japan's view, the OECD Arrangement appears to be an inappropriate reference in this proceeding. First, the OECD Arrangement does not cover agricultural products. Second, as Brazil recognizes elsewhere (in explaining its use of another outside index), the risks of financing arrangements for bulk agricultural commodity products, such as cotton, are not only substantial, but

[20] *Id*., para. 46, citing *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India*; *Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW (24 April 2003), para. 87.
[21] *EC – Bed Linens – 21.5 AB*, para. 87 (first emphasis in original; second emphasis added).
[22] *See* Brazil's First Submission, paras. 438 – 443, citing Exhibit Bra – 546 (OECD document TD/PG (2005) 38/FINAL, 5 December 2005).
[23] *See* U.S. First Submission, para. 60, quoting "Cotton: Review of the World Situation", ICAC, p. 11 (May – June 2006) (BRA – 485).
[24] *See* Brazil's First Submission, paras. 438 – 443.

also unique. Brazil notes that the tenor for Letter of Credit Insurance (LCI) granted by the Export-Import Bank of the United States (Ex-Im Bank) is capped at 180 days for bulk agricultural products.[25] Furthermore, the scope of application of the OECD Arrangement is export credits with repayment terms of two years or more. Thus, Brazil's use of the OECD Arrangement in this case is inappropriate.

26. Japan urges the Panel to closely examine Brazil's rationale for its use of the OECD Arrangement MPRs.

2. The U.S. Use of the International Cotton Advisory Committee Report

27. Japan also takes issue with the use by the United States of an ICAC report. The United States quotes the ICAC report for the proposition that, following the 1 July 2005 modifications, the U.S. government's export credit guarantee programs "'*comply with the WTO ruling*.'"[26]

28. The ICAC is not empowered to determine whether a WTO Member's measures comply with a WTO provision or whether changes to a non-compliant measure have brought the measure into compliance. Therefore, Japan is of the view that citations such as this are not relevant to the instant dispute.

29. Japan urges the Panel to closely examine the U.S. use of the ICAC Report.

III. CONCLUSION

30. Japan respectfully requests the Compliance Panel to examine carefully the facts and arguments presented by Brazil and the United States in light of the comments above, in order to ensure objective and consistent interpretation of the WTO agreements, particularly the ASCM and the DSU. We welcome any questions that the Panel may have regarding this submission.

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[25] *See* Brazil's First Submission, paras. 387 and 389.

[26] *See* U.S. First Submission, para. 60, quoting "Cotton: Review of the World Situation", ICAC, p. 11 (May – June 2006) (BRA – 485) (emphasis added by United States).

ANNEX A-10

THIRD PARTY SUBMISSION OF NEW ZEALAND

(5 January 2007)

CONTENTS

I. INTRODUCTION

1.01 The rulings and recommendations of the panel and of the Appellate Body in *United States – Subsidies on Upland Cotton* adopted by the Dispute Settlement Body ("DSB") on 21 March 2005 constituted an important step in the interpretation and application of the provisions of the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") in respect of both prohibited and actionable subsidies. In particular it clarified the meaning and scope of the concept of serious prejudice in Article 6 of the SCM Agreement. New Zealand was a third party in that case because of its systemic interest in the integrity of these provisions. As a leading agricultural exporter New Zealand has a particular interest in the application of the subsidies disciplines to agricultural products. Thus, New Zealand welcomed the adoption of the panel and Appellate Body reports.

1.02 Brazil now brings the matter of United States subsidies in respect of upland cotton back under Article 21.5 of the Dispute Settlement Understanding (DSU). Brazil argues that the United States action and inaction in respect of the recommendations and rulings of the DSB puts it in violation of its obligations under Articles 5 and 7.8 of the SCM Agreement. Failure by the United States to remove the adverse effects or withdraw the subsidising measures as required by Article 7.8 of the SCM Agreement, calls into question the very viability of the disciplines in that Agreement. As a result, New Zealand is exercising its right as a third party in this Article 21.5 compliance proceeding.

1.03 In New Zealand's view, the decision of the panel in this case will have far-reaching implications. Not only is the fact of non-compliance a threat to the subsidy disciplines of the SCM Agreement, but the arguments put forward by the United States in its response to the claim of Brazil have serious systemic implications for the future application of the SCM Agreement. New Zealand will elaborate on this aspect throughout this submission.

II. THE FINDINGS IN QUESTION AND THE ALLEGED MEASURES OF IMPLEMENTATION

2.01 In this submission New Zealand will focus on the implementation of the recommendations and rulings of the DSB in respect of the subsidies that were found by the panel in the original proceedings to be actionable. The relevant part of the panel's findings is paragraph 8.1(g)(i) which provides:

> the effect of the mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments - is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*;

2.02 In paragraph 8.3 the panel went on to say in respect of its finding in paragraph 8.1(g)(i), that in light of Article 7.8 of the SCM Agreement the United States was under an obligation to "take appropriate steps to remove the adverse effects … or withdraw the subsidy". The Appellate Body expressly upheld the finding of the panel in paragraph 8.1(g)(i).

2.03 As Brazil has pointed out, the only action taken by the United States in implementing the recommendations and rulings of the DSB on 21 March 2005 has been the abolition of user marketing (Step 2) payments. The programmes under the Farm Security and Rural Investment ("FSRI") Act of 2002 providing for marketing loan payments and counter-cyclical payments remain. Since these were the major contributors to the price suppression and hence the serious prejudice found by the panel then, as Brazil argues, the United States has failed to remove the adverse effects as required by Article 7.8 of the SCM Agreement and thus remains in violation of Article 5 of the SCM Agreement.

2.04 The United States response falls into two broad areas. First, the United States argues that certain claims made by Brazil are outside the scope of DSU Article 21.5 proceedings and requests that the panel make preliminary rulings to that effect. Second the United States claims that Brazil has failed to show that in the absence of the Step 2 payments, the marketing loan and counter-cyclical programmes cause serious prejudice either through price suppression or through an increase in world market share. In New Zealand's view both of these arguments are flawed. In this submission, New Zealand will provide some comments on the United States claims. In respect of the request for preliminary rulings, New Zealand will focus on the claim that the marketing loan and counter-cyclical programs are outside the scope of these Article 21.5 proceedings.

III. DSU ARTICLE 21.5 AND SCM AGREEMENT ARTICLE 7.8

3.01 Before addressing the United States preliminary rulings claim, New Zealand wishes to make some comments on the uniqueness of this case and the importance of its implications. This Article 21.5 proceeding involves for the first time the question of compliance in respect of the obligation under Article 7.8 of the SCM Agreement either to withdraw the subsidy or to "take appropriate steps to remove the adverse effects". Hence this panel is faced with the interpretation of both DSU Article 21.5 and Article 7.8 of the SCM Agreement and with determining their relationship to each other.

3.02 DSU Article 21.5 mandates a panel to consider "the existence or consistency of measures taken to comply with the recommendations and rulings" of the DSB. As the Appellate Body has pointed out, this provision entitles a panel to determine whether any measures exist to implement the recommendations and rulings of the DSB.[1] However, when compliance with Article 7.8 of the SCM Agreement is raised in an Article 21.5 proceeding, it is not just a question of the existence of measures or of their consistency with the recommendations and rulings of the DSB that has to be considered. If the subsidising measures in question have not been withdrawn then there is the further question of whether "appropriate steps" have been taken to remove the adverse effects of those measures.

3.03 In New Zealand's view, an enquiry to determine whether Article 7.8 of the SCM Agreement has been complied with can involve a panel in looking at three things. First, a panel must determine whether the subsidising measures have been withdrawn. Second, if those measures have not been withdrawn, then the panel must consider whether any steps have been taken to remove the adverse effects. Third, if the panel finds that steps have been taken to remove the adverse effects, then it must determine whether those steps are "appropriate".

3.04 In New Zealand's view, the steps would only be "appropriate" if they are capable of removing the adverse effects. The *Oxford English Dictionary* defines "appropriate" as meaning "specially fitted, suitable, proper".[2] A measure that is not capable of achieving its objective of removing the adverse effects would be neither suitable nor appropriate. As a consequence, steps taken by an implementing Member that are not capable of removing the adverse effects would not be "appropriate steps" within the meaning of Article 7.8 of the SCM Agreement.

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[1] Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, 14 March 2006, para. 93.

[2] *The Oxford English Dictionary* (2nd Edition) – Volume I, Clarendon Press, Oxford: 1989, p. 586.

IV. THE PRELIMINARY RULINGS CLAIM

4.01 The United States claims that marketing loans and counter-cyclical programmes under the FSRI are "outside the scope" of the Article 21.5 proceeding. The United States presents two arguments in this respect. First, it argues that the DSB ruling covered only certain "payments" under those programmes, not the programmes themselves. Second, the United States argues that these programmes do not constitute "measures taken to comply" with the recommendations and rulings of the DSB and hence they fall outside the scope of DSU Article 21.5. In New Zealand's view both arguments are unsupportable. Moreover, if these arguments were to be upheld, the actionable subsidy regime under the SCM Agreement would be completely undermined.

4.02 New Zealand notes that the United States also requests a preliminary ruling that Brazil's claim that no action was taken by the United States in implementation of the recommendations and rulings of the DSB between 21 September 2005 and 31 July 2006 is also outside the scope of these proceedings. On this matter, however, Brazil is undoubtedly correct. The United States cannot claim that since it took no implementing action until 1 August 2006, that period is outside the scope of these proceedings. DSU Article 21.5 applies to the "existence" of measures not just to the consistency of measures actually taken to comply with the recommendations and rulings of the DSB.

A. THE PAYMENTS/PROGRAMMES DISTINCTION

4.03 The United States claim that the panel's finding in paragraph 8.1(g)(i) is limited to specific payments and did not cover the programmes that authorise those payments involves a rewriting of the panel's findings. The United States seeks to revise the finding of the panel in light of certain arguments made by Brazil in the panel proceedings, but there is no justification for rewriting the conclusions of the panel in this way.

4.04 An examination of the panel's finding indicates that the United States contention simply has no basis. In paragraph 8.1(g)(i) the panel made a finding about "the effect of the mandatory price-contingent United States subsidy measures". The finding was that these measures constituted "significant price suppression". The descriptive reference to "marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments" does not alter the nature of the finding. Payments are not mandatory subsidy measures; they are simply the means by which the subsidy measures are implemented.

4.05 Moreover, it is quite clear that the panel's analysis of the subsidy measures that caused price suppression was of the programmes under the FSRI under which payments are made. The panel determined that the marketing loan payments are mandatory by reference to the "text of the measure".[3] The "measure" here is the marketing loan programme, not the payment itself. The panel states, "the structure, design and operation of the marketing loan programme has enhanced production and trade-distorting effects"[4]. Again, it is the programme under which the payments were made that was being considered by the panel, not just specific payments.

4.06 The United States claims that the statement of the panel in paragraph 7.1501 that "the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our ‘present' serious prejudice finding" is not a recommendation of the panel, and thus presumably is not binding on the United States. What this argument ignores, however, is that although not a recommendation as such, the statement is relevant to understanding the findings of the

[3] Panel Report, *United States – Subsidies on Upland Cotton* WT/DS267/R, 8 September 2004, paragraph 7.1291.

[4] *Ibid*, paragraph 7.1295.

panel. It gives meaning to the finding in paragraph 8.1(g)(i) relating to the "United States subsidy measures" that constituted significant price suppression.

4.07 In short, read properly in the context of the panel's decision as a whole, the finding in paragraph 8.1(g)(i) is not limited to the specific payments in MY 1999-2002. It applies to the measures under which those payments are authorised and hence to the marketing loan and counter-cyclical programmes themselves.

4.08 Moreover, the United States distinction between payments and programmes leads to an absurd result. It means that serious prejudice would have to be proved annually in the light of payments that have been made by which time the adverse effects have already occurred and it would be too late to withdraw the measure that caused them. To argue that the panel was referring only to payments in MY 2002 makes nonsense out the panel's own reference to Article 7.8 of the SCM Agreement and to the requirement to withdraw the subsidy. How can a subsidy be withdrawn if in fact the subsidy is over and the subsidizing effect is past? The United States arguments would simply undermine the disciplines on actionable subsidies in the SCM Agreement.

B. The "Measures taken to Comply" argument

4.09 The United States also argues that the marketing loan and counter-cyclical payments programmes are outside the scope of these Article 21.5 proceedings because they are not "measures taken to comply with the recommendations and rulings" of the DSB. According to the United States, "Article 21.5 applies only with respect to a disagreement as to the existence or consistency of a measure taken to comply", hence it cannot apply to programmes that existed at the time the matter came before the original panel and are unchanged. Under the United States logic, any such challenge to these measures has to be the subject of a new complaint.

4.10 In New Zealand's view, the United States argument ignores the fact that Article 21.5 is not the only relevant provision in these proceedings. In respect of the panel's finding under paragraph 8.1(g)(i), the obligation on the United States is found in Article 7.8 of the SCM Agreement. This provision grants the United States the choice either to withdraw the measures in question or to remove the adverse effects. Having chosen not to withdraw the marketing loan and counter-cyclical payments programmes, the United States cannot now avoid its obligation under Article 7.8 of the SCM Agreement to remove the adverse effects of those subsidy programmes by claiming that they are not measures taken to comply within the meaning of DSU Article 21.5. The United States cannot use the provisions of Article 21.5 to nullify its obligation under Article 7.8 of the SCM Agreement.

4.11 As pointed out in paragraphs 3.03 and 3.04 above, in applying Article 7.8 of the SCM Agreement to the present case the panel has to determine whether the measures causing serious prejudice have been withdrawn. In the case of the marketing loan and the counter-cyclical payments programmes they have not been withdrawn. The panel must then determine whether steps have been taken to remove the adverse effects found to exist by the original panel. It must then determine whether any steps that have been taken are "appropriate", that is whether they are measures that are capable of removing the adverse effects. DSU Article 21.5 cannot be invoked, as the United States seeks to do in this case, as a barrier to the panel conducting such an analysis.

V. THE SUBSTANTIVE CLAIMS

5.01 Brazil argues that even in the absence of the Step 2 payments programme, marketing loan payments and counter-cyclical payments alone cause significant price suppression. Indeed, Brazil argues that the removal of the Step 2 programme could increase counter-cyclical payments, thus adding to the significant price depression. Brazil also argues that marketing loan and counter-cyclical payments threaten to cause serious injury in MY 2006 and beyond. New Zealand supports these claims.

5.02 The United States response falls into three broad categories. First the United States argues that Brazil has not substantiated its claim that the effect of the Step 2 payments on price suppression was "relatively modest". Second the United States claims that Brazil is in effect arguing that the marketing loan and counter-cyclical payments *per se* violate the WTO Agreements, and that this could only occur if the programmes "mandate a breach" of those agreements, which the United States claims that they do not. Thirdly, the United States argues that Brazil has failed to make a *prima facie* case of the WTO inconsistency of the marketing loan and counter-cyclical payments programmes.

5.03 New Zealand will comment on each of these arguments, but before doing so will make a preliminary observation about the implications of the United States arguments in the context of an Article 21.5 case where the central question is whether there has been compliance with Article 7.8 of the SCM Agreement.

5.04 The essence of the arguments of the United States is that Brazil has the burden of showing that in the light of the removal of the Step 2 payments programme the marketing loan and counter-cyclical payments programmes cause or threaten serious prejudice, and it has failed to meet that burden. There is no doubt that as complainant in this Article 21.5 proceeding Brazil bears the burden of proof.[5] The question is what does such a burden entail?

5.05 In the present case, the DSB recommendations and rulings of 21 March 2005 covered three programmes; the Step 2 payments programme, the marketing loan payments programme and the counter-cyclical payments programme. But having chosen to remove only one of those programmes, the United States now claims that Brazil has the burden of showing that the remaining two programmes cause serious prejudice. Thus, in substance the United States is claiming that Brazil must prove again what it had already proved and what has been already been found by the original panel to cause serious prejudice. This cannot be the intent of either DSU Article 21.5 or Article 7.8 of the SCM Agreement. A Member should not have the burden of proving something that has already been decided by the original panel.

5.06 In New Zealand's view, Article 7.8 of the SCM Agreement operates to distribute the burden of proof somewhat differently. Since an implementing Member has the option of either withdrawing the subsidising measure or removing the adverse effects, a Member that fails to withdraw the measure in question then should have the burden of showing that it has removed the adverse effects. Thus, in the present case proof by Brazil that the measures found by the original panel to cause adverse effects have not been withdrawn should establish a *prima facie* case that implementation has not occurred and the burden should then shift to the United States to prove that the adverse effects caused by those subsidising measures have been removed.

A. THE UNITED STATES CLAIM THAT THE IMPACT OF THE REMOVAL OF STEP 2 PAYMENTS IS NOT "RELATIVELY MODEST"

5.07 Much of the United States argument that Brazil is incorrect in treating the impact of the removal of Step 2 payments as "relatively modest" is focused on what it perceived Brazil to be arguing before the original panel. But this is simply not relevant. Rather, it is what the panel decided and the actual impact of the removal of the Step 2 payment programme that is relevant. The original panel concluded that the marketing loan and counter-cyclical payments programmes contributed to

[5] Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, 25 April 1997, p. 14.

price suppression and serious prejudice. In its First Written Submission Brazil has demonstrated that notwithstanding the withdrawal of the Step 2 payments programme, payments under the marketing loan and counter-cyclical payments programmes caused price suppression in the world market in MY 2005 and an increase in United States world market share in upland cotton in MY 2005. Thus, there is serious prejudice within the meaning of SCM Article 5(c).

5.08 The United States claim about the significance of the removal of the Step 2 payments programme is undermined by a comparison of the amounts paid under the various programmes. Step 2 payments are small compared to marketing loan and counter-cyclical payments. In the most recent year, 2005, for example, the Step 2 payments amounted to US$350 million. In the same year, the marketing loan and counter-cyclical programme payments amounted to US$2,170 million.[6] Similar ratios existed in most other years. There is no doubt that the removal of the Step 2 payment programme had some impact, but the United States cannot ignore the much larger volume of subsidisation under the two programmes that have not been withdrawn or modified.

5.09 The United States also seeks to counter Brazil's argument that eliminating Step 2 payments could result in a higher counter-cyclical payment rate by arguing that in the current year there could not be any increase in counter-cyclical payments. But, this is because counter-cyclical payments are already at their maximum rate.[7] In other words, the United States is not arguing that the counter-cyclical programme would not compensate for the elimination of the Step 2 payments; rather, it is arguing that payments are already so high that under current conditions no further payments can be made. None of this supports the United States contention that the programme does not have a price suppressing effect.

5.10 The United States also contends that Brazil fails to recognize that the elimination of Step 2 payments will result in a lowering of marketing loan payments. While this may be true because marketing loan payments are configured on world prices, which would increase with the elimination of Step 2 payments, what the argument ignores is the fact that these programmes are distorting whether or not payments are made under them. It is the programmes themselves not the payments that create expectations. Producers know that the loan rate is there to support them, that there is a target price[8] that they will receive either from the market or from the government. Neither the elimination of Step 2 payments nor any lowering of marketing loan payments in fact diminishes the distorting effect of the marketing loan and counter-cyclical programmes.

5.11 Finally, even the United States own figures show that the impact of the elimination of the Step 2 payment programme is modest. On one occasion it cites an increase of 0.4c/lb in the adjusted world price or $2.25 per ha[9] and on another occasion it cites an increase in the world price of 1.4c/1b or $2.30 per ha.[10] By comparison with the futures price in 2005-2006 (52.9-59.35 cents per pound)[11], loan rate (52 cents per pound)[12] or target price in the same period (72.4 cents per pound)[13], this effect on world prices of the elimination of the Step 2 payment programme is indeed "relatively modest".

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[6] *United States – Subsidies on Upland Cotton – Recourse by Brazil to Article 21.5 of the DSU* (DS267), First Written Submission of Brazil, 17 November 2006, ("Brazil First Written Submission"), para. 111, and Table 6.

[7] *United States – Subsidies on Upland Cotton – Recourse by Brazil to Article 21.5 of the DSU* (DS267), First Submission and Request for Preliminary Rulings of the United States, 15 December 2006, ("United States First Written Submission"), para. 162.

[8] United States First Written Submission, para. 161.

[9] United States First Written Submission, para. 174.

[10] United States First Written Submission, para. 169.

[11] United States First Written Submission, para. 231.

[12] *Ibid*.

[13] United States First Written Submission, para. 161.

5.12 The United States arguments leave intact the fundamental point made by Brazil, that even in the absence of the Step 2 payment programme, the marketing loan and counter-cyclical programmes still result in significant price suppression within the meaning of Article 6.3(c) of the SCM Agreement and thus cause serious prejudice contrary to Article 5(c) of the SCM Agreement.

B. THE UNITED STATES CLAIM THAT MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS PROGRAMMES DO NOT MANDATE A BREACH OF THE WTO AGREEMENTS

5.13 The United States claims that Brazil cannot challenge the marketing loan and counter-cyclical payments programmes unless it can show that these programmes mandate a breach of the WTO agreements. In the United States view, to do so Brazil would have to show that these programmes mandated actions that must lead to the effect of causing serious prejudice to Brazil, and Brazil has not done so.

5.14 Once again, the United States is ignoring the fact that the original panel had already determined that payments under the programmes in question caused serious prejudice to Brazil. Equally, the United States is ignoring the fact that the question in this case is not whether the programmes in question require that adverse effects are caused to Brazil, but whether the United States has taken appropriate steps to remove the adverse effects found by the original panel to exist as a result of the operation of these programmes. In this context, the mandatory/discretionary distinction called in aid by the United States is simply irrelevant.

C. THE UNITED STATES CLAIM THAT BRAZIL HAS FAILED TO MAKE A *PRIMA FACIE* CASE OF WTO INCONSISTENCY OF THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS PROGRAMMES

5.15 As pointed out earlier, the United States arguments on the WTO-consistency of the marketing loan and counter-cyclical payments programmes are tantamount to placing on Brazil a burden to prove once again what it had already proved before the original panel. In New Zealand's view such an approach to the application of Article 7.8 of the SCM Agreement risks depriving the actionable subsidies provisions of the SCM Agreement of their proper effect. Furthermore, New Zealand sees many of the arguments of the United States as attempts to reargue what it argued before the original panel, and lost. Again, such an approach is consistent with the objectives of neither DSU Article 21.5 nor Article 7.8 of the SCM Agreement.

1. Counter-cyclical Payments

5.16 The United States attempts to counter Brazil's arguments about the trade-distorting effects of counter-cyclical payments by blurring the line between counter-cyclical payments and decoupled payments. Thus, it cites studies relating to decoupled payments and says that they provide "valuable insights".[14] The United States also refers to studies concerning general wealth risks[15], as if they were equally applicable to the revenue risk that counter-cyclical payments are concerned with, again treating counter-cyclical payments as co-extensive with decoupled payments. But counter-cyclical payments are not real decoupled payments.

5.17 Real decoupled payments are green box measures and as defined in Annex 2 of the Agreement on Agriculture cannot be linked to the type or volume of production (paragraph 6(b)), or be related to or based on prices (paragraph 6(c)). Counter-cyclical payments, by contrast, are clearly and explicitly linked to prices. The fact that in many years such payments are likely to be paid out at

[14] United States First Written Submission, para. 213.
[15] United States First Written Submission, para. 209.

the maximum rate[16] does not change the fact that they are linked to prices. The question is what would farmers do differently if there were no counter-cyclical payments and farmers were, essentially, "guaranteed" 13.73c/lb less for their cotton? Counter-cyclical payments are clearly not green box measures and hence are presumptively trade distorting.

5.18 The same fallacy of linking counter-cyclical payments to decoupled payments is found in the United States arguments about the increase in wealth from counter-cyclical payments accruing to non-operator landlords and hence capitalised into higher land values.[17] While this is certainly true of real decoupled payments, it is simply not plausible in the case of counter-cyclical payments. What producer is going agree to the "modified rental arrangements" that the United States refers to[18], when counter-cyclical payments could be at 13.73 c/lb one year and at zero the next?

2. Marketing Loan Payments

5.19 The United States claims that Brazil has failed to demonstrate that marketing loan payments are having significant price-distorting effects. Yet the proposition that marketing loan payments are distorting is almost self-evident. Marketing loan payments are amber box measures, the category in which are included the non-prohibited measures with the most distorting effect on production and trade.

5.20 Moreover, the United States arguments about marketing loan payments ignore once again that it is the expectations of producers that are important and that those expectations are generated because of the existence of the applied administrative prices under the marketing loan programme, not because of the financial transfers in any year. Thus, the United States argument that since cotton futures prices in MY 2006 were higher than the loan rate then the loan rate would have no effect on producers planting decisions[19] misses the point. First, the loan rate will not always be below the futures prices; in some years there have been large amounts paid out under the marketing loan programme.[20] Second, the programme offers a guarantee by the government that producers will receive a particular price whether they are involved in the futures market or not.

5.21 Furthermore, the United States claims that at the time of planting producers "*did not expect*" that they would receive these payments on harvest[21] is a clever play on the word "expect". No doubt producers hoped that they would receive a higher price. But what they certainly expected was that they would receive at least the guaranteed price of 52c/lb, regardless of what happened in the market place, because that is what the law mandated. As the Appellate Body pointed out in the original proceeding[22]:

> … although farmers had expected higher prices in making their planting decisions, they were also aware that if actual prices were ultimately lower, they would be "insulated"[23] by government support, including not only marketing loan program payments but also counter-cyclical payments, …

[16] United States First Written Submission, para. 211.
[17] United States First Written Submission, paras. 216-219.
[18] United States First Written Submission, para. 216.
[19] United States First Written Submission, para. 230.
[20] United States First Written Submission, para. 248.
[21] United States First Written Submission, para. 231. (Emphasis in original.)
[22] Appellate Body Report, *United States – Subsidies on Upland Cotton*, 3 March 2005, WT/DS267/AB/R, ("*U.S. – Upland Cotton (AB)*"), para. 445.
[23] Panel Report, *United States – Subsidies on Upland Cotton*, 8 September 2004, WT/DS267/R, ("*U.S. – Upland Cotton (Panel)*"), para. 7.1294.

5.22 Thus, it was the guarantee of insulation that was affecting planting decisions – whether the price was received from the market or the government was immaterial. In fact, it is most unlikely that the farmers give the same weight to futures prices as to the guaranteed loan rate. To do so would require them to sell all their crops forward at the future rate and take the risk that their actual production would allow them to meet their forward commitments – in effect to take the production risk from which marketing loan programme payments based on actual production was protecting them.

3. Marketing Loan and Counter-Cyclical Payment Programmes and Market Signals

5.23 Much of the United States argument is directed to trying to demonstrate a link between producer decisions and market signals. However, the United States does not and cannot demonstrate that planting decisions of producers were shaped by market factors. The United States failed to do so before the original panel and the Appellate Body, and its attempt to reargue the matter in these Article 21.5 proceedings is equally ineffective.

5.24 The United States argues that the fact that the United States share of production has been stable over the life of the marketing loan and counter-cyclical programmes indicates that the programmes are not insulating producers from market signals.[24] But, the question is not whether United States share of production has been stable it is whether in the absence of the marketing loan and counter-cyclical payments programmes the United States market share would be at current levels. And the answer to that question would have to be no. The United States says that Brazil's claim that "*But for* the effect of price-contingent U.S. marketing loan and counter-cyclical payments, it would be expected that non-subsidized producers, such as those in Brazil and West and Central African countries, would have significantly increased their share of production and exports in the world market"[25] simply assumes its own conclusion.[26] But this is just assertion not argument, and thus the United States has no response to Brazil's position.

5.25 The United States argues that there is an inconsistency between Brazil's assertion that there is no link between prices and United States acreage, production and exports, and its claim that the United States is the single most important market influencing world market prices.[27] If the United States is the single most important market influencing world prices, the United States says, then surely there must be a link between world prices and United States planted acreage, production and exports. But the inconsistency is of the United States own making. The link is not between world prices and United States production. It is between domestic, guaranteed prices and United States production. And, that of course, is the source of the problem.

5.26 The United States claim that at the time of planting a farmer "cannot *know* what final prices and final costs will be,"[28] says less than meets the eye. What the farmer does know is that for all cotton harvested the price will be at least the loan rate. In addition, if market price is not significantly above the loan rate and the planting is on base acres there will be a counter-cyclical payment top-up (albeit based not on actual production, but on average yields in earlier years). So, if the farmer continues to produce cotton the expected return is going to be around the target price for most production on base acres. By contrast, cotton producers in Africa or Brazil know that they will get only the world price – whatever that is.

[24] United States First Written Submission, para. 243.
[25] Brazil First Written Submission, para. 90.
[26] United States First Written Submission, para. 251.
[27] United States First Written Submission, para. 254.
[28] United States First Written Submission, para. 255. (Emphasis in original.)

5.27 The United States contests Brazil's claim that the marketing loan and counter-cyclical payments programmes play an essential role in ensuring that producers cover their long-term costs of production and that in the absence of these programmes producers would switch to alternative crops.[29] It is, in the United States view, variable costs not long-term costs that influence the decision on whether to continue or exit cotton farming. However, the United States claim that Brazil has provided no evidence that absent the payments farmers would exit cotton production[30] ignores the evidence that Brazil provides in fact.

5.28 In paragraph 11 of its First Written Submission, Brazil provides a table indicating total United States subsidies for upland cotton from MY 1999 to the present which demonstrates that in some years over half of the revenue received by United States cotton farmers comes from subsidies. The idea that if these subsidies were not there, producers who have been deprived of half of their income would carry on planting cotton – business as usual – is little short of absurd. Brazil also points out that without marketing loan and counter-cyclical payments between MY 2000-2005 United States cotton producers would have lost US$663 per acre.[31] No rational economic operator would continue to plant cotton under such conditions.

5.29 Furthermore, the United States claims that a substantial number of producers would not be affected by a reduction or elimination of payments because they plant on farms with no base acres or plant in excess of a farm's base acres[32], presents only part of the picture. While base acre yields are the basis for determining eligibility for counter-cyclical payments, they are irrelevant for determining marketing loan payments. So the producers who the United States claims would not be affected by the reduction or elimination of payments would in fact miss out on marketing loan payments if they were reduced or eliminated.

4. The Reliability of the Econometric Modelling

5.30 The United States claims that the econometric modelling provided by Brazil is flawed, but the United States arguments are either an attempt to reargue what was litigated before the original panel and the Appellate Body and lost, or are inconsequential. New Zealand will offer a few observations on the United States claims in this regard.

5.31 The United States makes much of the fact that in his new model Dr. Sumner has increased his United States cotton supply elasticity to 0.8.[33] However, as an alternative model to capture long run effects the United States proposes the ATPSM model which also has a United States cotton supply elasticity of 0.8![34] Moreover, the United States conveniently ignores footnote 301 in Brazil's submission[35] where it is stated "Brazil notes that Professor Sumner also ran 12 simulations using an even more conservative supply elasticity of 0.5. The results of this exercise demonstrate the robustness of the supply and price effects…."

5.32 The United States criticises Dr. Sumner for making a small change to the rest of the world (ROW) demand elasticity, -0.2 as opposed to -0.25. But this 0.05 change is a small change in relation

[29] United States First Written Submission, para. 292.
[30] United States First Written Submission, para. 297.
[31] Brazil First Written Submission, para. 158.
[32] United States First Written Submission, para 298.
[33] Brazil First Written Submission, Annex I, paras. 10-21.
[34] United States First Written Submission, Annex I, Table A7.
[35] Brazil First Written Submission, para. 171.

to the alternatives that the United States then offers, i.e. a range of 0.45 between different scenarios.[36] How can the United States claim that its own estimates have a more solid statistical basis than those used by Dr. Sumner? In fact, Dr. Sumner's demand elasticities are little different from those he used in the earlier proceeding, which were implicitly found to be credible by the original panel and Appellate Body.

5.33 Although the United States notes that the coupling factor used by Dr. Sumner is the same as the one he used in his original model[37], it then goes on to criticize the size of that factor. Once again, the United States is attempting to relitigate what had already been found to be credible by both the panel and Appellate Body in the original proceeding. In any event, while the price effects are not enormous under the United States parameters, the effect on exports - especially in the long-term – certainly is.

5. Increase in the World Market Share

5.34 The United States contests Brazil's claim that the effect of the marketing loan and counter-cyclical payments programmes is to increase the United States world market share in upland cotton and hence constitutes serious prejudice within the meaning of Article 6.3(d) of the SCM Agreement. But in seeking to show that there has been no increase in United States market share, the United States is once again addressing the wrong question.

5.35 The essence of Brazil's argument is that the United States market share is higher than it would otherwise be and that this is because of the marketing loan and counter-cyclical payments programmes. Thus, the United States arguments that its market share has not increased over the period in question are simply not relevant. Moreover, the United States own analysis proves Brazil's point. In its critique of Dr. Sumner's analysis, the United States indicates that the long-term effect of the elimination of marketing loan and counter-cyclical payments would be a reduction in United States cotton exports of up to 25 per cent in 2002-2005 and 17 per cent in 2006-2008.[38] That is a very clear measure of what United States world market share would be in the absence of the marketing loan and counter-cyclical payments programmes.

5.36 In short, the United States itself makes the *prima facie* case under Article 6.3(d) of the SCM Agreement that it claims that Brazil has been unable to make.

VI. CONCLUSION

6.01 In conclusion, in New Zealand's view, Brazil has demonstrated that the United States has failed either to withdraw the marketing loan and counter-cyclical payments programmes or to remove the adverse effects of those programmes as required by Article 7.8 of the SCM Agreement. Accordingly, the United States has failed to comply with the recommendations and rulings of the DSB of 21 March 2005.

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[36] The ROW demand elasticities used by the United States range from -0.39 to -0.84. United States First Written Submission, Annex I, Table A7.

[37] United States First Written Submission, Annex I, para. 31.

[38] United States First Written Submission, Annex I, Table A8.

ANNEX B

REBUTTAL SUBMISSIONS OF THE PARTIES

ANNEX B-1

EXECUTIVE SUMMARY OF THE REBUTTAL SUBMISSION OF BRAZIL

(Executive summary submitted on 18 January 2007)

1. Brazil's First Written Submission set out its claims regarding the existence and consistency of United States ("U.S.") measures taken to comply with the adverse effects- and export subsidy-related recommendations and rulings of the Dispute Settlement Body ("DSB") in this dispute. In its Rebuttal Submission, Brazil demonstrates that none of the arguments raised by the United States in its First Written Submission has merit or rebuts Brazil's claims.

ADVERSE EFFECTS-RELATED ARGUMENTS

2. With respect to the adverse effects-related arguments, Brazil addresses, first, four issues raised by the United States that cut across all of Brazil's adverse effects-related claims. Brazil then rebuts the substantive arguments raised by the United States.

3. *First*, the United States asserts that the appropriate year for the compliance Panel to consider is marketing year ("MY") 2006. Brazil disagrees. The compliance Panel should conduct its analysis of Brazil's claims based on MY 2005, the most recent marketing year for which complete data is available. The United States assertion that MY 2006 is a more appropriate year contradicts the United States' own view in the original proceeding that the most recent period for which complete data are available is the appropriate period.

4. *Second*, the United States challenges, either directly or indirectly, a number of findings of the original panel regarding both the nature and the effects of the U.S. marketing loan and counter-cyclical subsidies and the nature and extent of the influence of U.S. production and exports on the world market price of upland cotton. In assessing Brazil's serious prejudice claims, the compliance Panel should rely on the findings of the original panel and Appellate Body. Article 21.5 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU") is not intended or designed to allow a Member to re-litigate findings by the original panel, as upheld by the Appellate Body.

5. *Third*, the United States argues that Brazil is raising an "as such" claim against the U.S. marketing loan and counter-cyclical payment programs, and that Brazil has failed to demonstrate that these programs mandate a breach of Articles 5 and 6.3 of the *Agreement on Subsidies and Countervailing Measures* ("*SCM Agreement*"). However, Brazil's claims do not distinguish between the adverse effects caused by the statutory and regulatory framework of the programs under the Farm Security and Rural Investment Act ("FSRI Act") of 2002, and the adverse effects caused by the mandatory and price-contingent payments flowing therefrom. Instead, Brazil's claims concern the adverse effects caused by U.S. "subsidies," in terms of their "effects" on U.S. production, exports and the world market price of upland cotton. This approach is consistent with the provisions of Part III of the *SCM Agreement* and the original panel's findings.

6. *Fourth*, the United States asserts that it did not have sufficient time to respond to Brazil's threat of serious prejudice claims and that it will respond in its forthcoming submission. This unilateral decision by the United States violates the *Working Procedures of the Panel* and prejudices Brazil's ability to rebut such U.S. arguments. Brazil requests that the compliance Panel reject any

factual evidence and accompanying arguments submitted in the U.S. rebuttal submission regarding Brazil's claims that if faces a threat of serious prejudice.

7. Turning to the substantive issues regarding Brazil's adverse effects-related claims before the compliance Panel, the United States first asserts that the removal of the Step 2 subsidy is sufficient to remove the adverse effects caused by the price-contingent subsidies under the FSRI Act of 2002. This U.S. argument implies that the Step 2 subsidy – but *not* the marketing loan or counter-cyclical subsidies – was *the sole* cause of the serious prejudice found by the original panel and Appellate Body to exist during the period MY 1999-2002, as well as the *sole cause* of any serious prejudice that resulted from these three subsidies under the FSRI Act of 2002 during the period MY 2003-2005. It also implies that the United States considers the far larger and more trade-distorting marketing loan and counter-cyclical subsidies, which accounted for 42 percent of the market value of upland cotton production in Marketing Year ("MY") 2005, to have no production, export or world price effects. Much of Brazil's rebuttal submission demonstrates that this argument is false. Marketing loan and counter-cyclical payments insulate U.S. producers from market forces, maintain high levels of upland cotton planted acreage, production and exports and significantly suppress world market prices.

8. The United States argues at length that the repeal of the Step 2 subsidy will not increase counter-cyclical payments in MY 2006 and will reduce marketing loan payments. The United States also asserts that, since counter-cyclical subsidies are currently at their maximum level, they will not increase in the forthcoming year. However, studies by both the Food and Agriculture Policy Research Institute ("FAPRI") and a U.S. government agency reveal that the repeal of the Step 2 subsidy will not cause any meaningful reduction in U.S. marketing loan subsidies. Moreover, the United States argument that counter-cyclical subsidies will be at there maximum, if anything, demonstrates that the removal of the Step 2 subsidy will be insufficient to remove adverse effects. An examination of U.S. upland cotton producers' revenue demonstrates the critical importance of marketing loan and counter-cyclical payments relative to Step 2 payments. While the elimination of Step 2 payments is expected to reduce upland cotton producer's revenue by $9 per acre per year, marketing loan payments and counter-cyclical payments provided U.S. upland cotton producers with revenue of $84 per acre and $75 per base acre, respectively, in MY 2005.

9. The United States argues that the decline in U.S. exports in the beginning of MY 2006 demonstrates that the removal of the Step 2 subsidy had a large impact. The decline in U.S. exports in the first few months of MY 2006 can largely be explained by market conditions. Any additional decline from the elimination of Step 2 payments is the result of a temporary surge of exports preceding the elimination of Step 2 subsidies and a subsequent lull following Step 2's elimination. Domestic mill users and exporters naturally sought to take advantage of a lucrative export subsidy while it lasted. However, USDA predicts U.S. exports to increase significantly in the remainder of MY 2006. Indeed, USDA predicts U.S. upland cotton exports will be the second largest on record in MY 2006, slightly less than the record established in MY 2005.

10. Finally, contrary to the United States' assertion, Brazil's arguments about the effect of Step 2 payments before this compliance Panel are consistent with Brazil's position before the original panel and Appellate Body. The Step 2 subsidy had two principal effects. One was to increase upland cotton producers' revenue. However, this effect was indirect and much less important in stabilizing upland cotton producers' revenue than the far larger marketing loan and counter-cyclical subsidies. A second effect of the Step 2 subsidy was to make U.S. upland cotton competitive in the world market at all times, thereby suppressing world market prices. While the elimination of the Step 2 subsidy eliminated this second effect, upland cotton producers' revenue is still insulated from market prices by marketing loan and counter-cyclical subsidies. Thus, Brazil's assertion that the elimination of the Step 2 subsidy will have a relatively modest impact on the volume of U.S. upland cotton production and exports is consistent with a finding that the elimination may also increase world market prices.

11. In its First Written Submission, the United States addresses some of Brazil's arguments establishing a causal link between marketing loan and counter-cyclical subsidies and significant price suppression in the world market for upland cotton.

12. *First*, ignoring the findings of the original panel, the United States argues that marketing loan and counter-cyclical payments have no significant production, export or price effects. The derelict U.S. argument that upland cotton producers do not expect to receive marketing loan payments was rejected by both the original panel and Appellate Body. Brazil demonstrates that *U.S. producers have expected to receive marketing loan payments every year since MY 1999.* The United States makes similarly shoddy arguments with respect to the effect of counter-cyclical payments. Economic literature confirms that counter-cyclical payments are trade-distorting and not generally capitalized into land values. Finally, the (incomplete) data on base and planted acreage presented by the United States confirms that U.S. farmers continue to overwhelmingly plant upland cotton on upland cotton base acreage. Over 95 percent of farms that grow upland cotton receive upland cotton counter-cyclical payments.

13. *Second*, the United States argues that Brazil solely characterizes the size of marketing loan and counter-cyclical payments as "large," "very large," "huge" and "massive," but does not address their structure, design or operation. This assertion is baseless. Brazil established the structure, design and operation of marketing loan and counter-cyclical payments in Section 7.8 of its First Written Submission. In rebutting the U.S. arguments, Brazil elaborates on this further. Furthermore, the magnitude of U.S. subsidies was an important factor in the original panel's price suppression analysis and continues to be an important factor before this compliance Panel.

14. *Third*, relying on the stable U.S. share of world production and exports, the United States argues that U.S. upland cotton producers are not insulated from market prices. The United States' arguments ignore, and effectively ask this compliance Panel to overturn, one of the central findings of the original panel and the Appellate Body – that the structure, design, and operation of the marketing loan and counter-cyclical subsidies "insulates" U.S. upland cotton producers from market forces by stabilizing their revenue at very high levels and allow them to sustain artificially high levels of planted acreage, production and exports.

15. *Fourth*, the United States argues that there is no connection between large marketing loan and counter-cyclical payments and increased U.S. production of upland cotton. Instead, the United States asserts that the increase can be attributed to high yields. Brazil disagrees. But for the challenged subsidies, no increased yields would have been harvested (because no upland cotton would have been planted) on a significant portion of U.S. upland cotton acreage. This would have resulted in a significant drop in overall U.S. planted acreage, production and exports.

16. *Fifth*, the United States argues that Brazil has failed to demonstrate a temporal coincidence between marketing loan and counter-cyclical subsidies and suppressed world market prices. While many of the same factors relied on by the original panel to make this determination exist today (*i.e.*, increasing absolute levels of U.S. production and exports), other factors, such as the U.S. share of world production and exports and prices have been relatively stable under the FSRI Act of 2002. However, this stability does not indicate that marketing loan and counter-cyclical subsidies have little or no effects. Rather, the constant stream of payments from these two mandatory, price-contingent subsidies has *maintained* existing significant price suppression. It is remarkable that the United States would assert that this relatively stable state of affairs – which continues only because of the United States' failure to implement the recommendations and rulings of the DSB – somehow reflects the *absence* of a causal link between these subsidies and significant price suppression. Indeed, Brazil's very claim in these proceedings is that the U.S. marketing loan and counter-cyclical subsidies have not changed, and continue to cause serious prejudice to the interests of Brazil.

17. *Sixth*, the evidence before the compliance Panel shows that the average upland cotton producer continues to be unable to cover its long-term total production costs with market revenue. While the United States acknowledges that producers must cover their total costs in the long term, the United States asserts that upland cotton farmers cross-subsidize upland cotton production with returns from other crops and off-farm revenue. Just as this argument was rejected by the original panel, so it should be rejected by the compliance Panel. Furthermore, an examination of the United States Department of Agriculture ("USDA") cost of production data demonstrates that a significant portion of U.S. upland cotton producers are unable to, and do not expect to, cover even their variable costs of production, when adjusting for the improper U.S. definition of variable costs. This suggests that, even in the short term, a significant portion of U.S. upland cotton production is not economically viable without marketing loan and counter-cyclical payments. Finally, the International Cotton Advisory Committee ("ICAC") comparison of production costs in different countries does offer further confirmation that U.S. upland cotton farmers are high cost producers.

18. *Seventh*, the United States criticizes the results of the study by Professor Daniel Sumner, presented in Brazil's First Written Submission, as overstated and inconsistent with economic literature. However, a single study from the U.S. Journal of Cotton Science cited by the United States provides no basis for this compliance Panel to ignore the substantial academic literature in agricultural economics that finds large world market price effects arising from U.S. cotton subsidies. Indeed, the general consensus of the economic literature is that U.S. cotton subsidies increase production and exports and drive down the world price of cotton. While studies find effects of different magnitudes based on different assumptions, many economists agree that world prices would be some 10 to 25 percent higher in the absence of cotton subsidies. As the largest subsidizing country in the world, the United States accounts for the majority of these effects. These results are consistent with and confirmed by Professor Sumner's 2003 and 2006 analyses.

19. *Eighth*, whether Chinese supply, as the United States argued in the original proceeding, or Chinese demand, as the United States currently argues, is responsible for certain price movements in the world market for upland cotton is irrelevant to Brazil's claim. What is important is whether large reductions in U.S. production and exports following a removal of marketing loan and counter-cyclical subsidies would result in significantly higher prices in the world market for upland cotton. The original panel found that the United States had a substantial proportionate influence on prices in the world market for upland cotton. Nothing has changed in this respect. Large amounts of U.S. upland cotton continue to be produced and exported to world markets. China's emergence as a large importer of upland cotton does not in any way alter this dynamics.

20. *Finally*, the U.S. arguments do not refute the strong *prima facie* case that marketing loan and counter-cyclical payments resulted in an increased U.S. world market share of production, as established in Brazil's First Written Submission. The United States does not dispute that there has been an increase in the U.S. world market share of production in MY 2005, as compared to the three year average in MY 2002-2004. Further, the evidence shows that *but for* the marketing loan and counter-cyclical payments in MY 2005, the U.S. market share would not have increased, but, rather, would have fallen sharply. Finally, none of the alternative periods offered by the United States to assess a consistent trend of increased market share covers periods relevant to an assessment of how the two subsidies at issue in this dispute – marketing loan and counter-cyclical subsidies (or their predecessors) – distort U.S. production, exports, and the U.S. world market share of production.

EXPORT SUBSIDY-RELATED ARGUMENTS

21. In its First Written Submission, Brazil demonstrated that the United States' "measures taken to comply" with the DSB's export credit guarantee ("ECG")-related recommendations do not exist in some respects, and to the extent they do exist, are not consistent with Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*. As a result, the

United States has failed to implement the DSB's recommendation that it withdraw the prohibited ECG-related subsidies without delay, under the *SCM Agreement*, and otherwise bring itself into conformity with its obligations, under the *Agreement on Agriculture*.

22. In its First Written Submission, the United States challenges Brazil's claim that, following adoption of the United States' implementation measures, ECGs extended under the General Sales Manager 102 ("GSM 102") program still constitute export subsidies. In so doing, the United States wildly overstates the impact of its limited ECG-related "measures taken to comply" with the recommendations and rulings of the DSB in this dispute. None of the facts highlighted by the United States demonstrates that the GSM 102 program, as amended by the United States' measures taken to comply: (i) results in the provision of GSM 102 ECGs on terms that are consistent with market; (ii) results in premium rates which are adequate to cover the program's long-term operating costs and losses; or, (iii) avoids circumvention of the United States' export subsidy commitments.

23. The United States raises five principal arguments in its First Written Submission. Brazil addresses each of these arguments below.

24. *First*, the United States asserts that Brazil may not, in these Article 21.5 proceedings, challenge the United States' application of GSM 102 in a manner that results in circumvention of U.S. export subsidy commitments for pig meat and poultry meat. The United States asks for a preliminary ruling from the compliance Panel in this regard. Brazil did not address the United States' request in this Rebuttal Submission, but instead replied to the U.S. arguments in a further submission on 16 January 2007.

25. *Second*, the United States asks the compliance Panel to reject Brazil's claim that no measures taken to comply exist with respect to ECGs issued under the GSM 102, General Sales Manager 103 ("GSM 103") or Supplier Credit Guarantee ("SCGP") programs prior to 1 July 2005, but still outstanding subsequent to that date, for two reasons: (a) a finding by the compliance Panel would be moot with respect to SCGP ECGs issued prior to 1 July 2005, since the maximum tenor for a SCGP ECG is 180 days and no such ECGs are therefore still outstanding; and, (b) the recommendations and rulings of the DSB required the United States to "withdraw the subsidy," which the United States asserts it has effectively accomplished by changing the fee structure for GSM 102 and halting the issue of GSM 103 and SCGP ECGs.

26. Given the impact of "reschedulings" of debt guaranteed by the program, SCGP ECGs issued prior to 1 July 2005 may well still be outstanding today. Also, ECGs outstanding subsequent to 1 July 2005 were issued under the fee schedule on which the original panel and the Appellate Body based a finding of export subsidization under item (j) of the Illustrative List of Export Subsidies in Annex I to the *SCM Agreement* ("item (j)"), and therefore form an essential part of the recommendation to "withdraw the subsidy." Payments or performance under those outstanding ECGs is inconsistent with the DSB's recommendation to "withdraw the subsidy."

27. *Third*, the United States asserts that item (j) constitutes the exclusive test to determine whether an ECG program constitutes an export subsidy. The United States is essentially proposing an *a contrario* reading of item (j), under which proof that the GSM 102 program meets its long-term operating costs and losses would render the program immune from challenge as an export subsidy under the elements of Articles 1.1 and 3.1(a) of the *SCM Agreement*.

28. The interpretation offered by the United States is not supported by footnote 5 to the *SCM Agreement*; proving that GSM 102 charges fees sufficient to meet its long-term operating costs and losses would not absolve the United States of the obligation to abstain from providing *de jure* export-contingent GSM 102 ECGs at fees that confer "benefits" on U.S. exporters (to the extent doing so circumvents U.S. export subsidy commitments under the *Agreement on Agriculture*). Moreover,

available data does not demonstrate, as the United States asserts, that the ECG programs are profitable. The GSM 102 program is not structured, designed or operated to meet the long-term operating costs and losses of the programs.

29. *Fourth*, the United States appears to assert that, even if the definition of export subsidy in Articles 1.1 and 3.1(a) of the *SCM Agreement* applies to ECGs, the only applicable standard to determine whether a "benefit" is conferred, within the meaning of Article 1.1(b), is the standard embodied in Article 14(c) of the *Agreement*. Article 14(c) calls for an assessment of the impact of a government guarantee on the cost of an underlying loan, relative to the cost of the loan without the guarantee.

30. The United States argues that Brazil's approach, which consists of comparing GSM 102 fees with fees for comparable (albeit also non-market) products offered by the United States Export-Import Bank ("ExIm Bank"), does not constitute a "marketplace" comparison, since in this context, the "marketplace" contemplated under the *SCM Agreement* is not the cost of obtaining a guarantee for a one-off transaction on the export of agricultural commodities, but rather the total cost of funds at which borrowers and lenders are willing to enter commercial loans. The United States then asserts, on the basis of three examples, that commercial lenders provide loans to CCC-approved foreign obligors on better terms than available under the GSM 102 program.

31. In arguing that Article 14(c) is the exclusive standard by which to assess whether a "benefit" is conferred by a guarantee, the United States fails to recognize that there are a number of potential benefits and beneficiaries in a transaction supported by a GSM 102 ECG: the U.S. exporter; the U.S. bank; the foreign bank (referred to by Brazil as the "foreign obligor"); and the foreign purchaser/borrower. In undertaking a comparison between GSM 102 fees and fees for comparable ExIm Bank products, Brazil is undertaking to assess a severable "benefit" to the U.S. exporter. The U.S. exporter does not bear the costs or risks of securing or extending financing to the foreign bank or the foreign purchaser/borrower. Indeed, that is the entire point of GSM 102 – it takes the U.S. exporter out of the equation. Thus, the benefit to the U.S. exporter can be measured through an assessment of how GSM 102 fees line up against the fees for similar instruments.

32. Further, the three examples offered by the United States – without any reference to primary documents and based solely on a 2-page letter from an officer of a U.S. bank that participates in the GSM 102 program – do not demonstrate that the GSM 102 program is consistent with market even under the standard in Article 14(c).

33. *Fifth*, the United States argues that, in asserting that GSM 102 ECGs are unique financing instruments with no parallel at market, Brazil failed to consider certain products offered by the Inter-American Development Bank ("IDB"), the International Finance Corporation ("IFC"), and the European Bank for Reconstruction and Development ("EBRD"). The United States also suggests that Brazil should not have restricted its "benefit" assessment to a comparison between GSM 102 fees and fees for similar ExIm Bank products, but instead should also have compared GSM 102 fees to fees for IDB, IFC and EBRD products.

34. Consideration of the IDB, IFC and EBRD products discussed by the United States does not affect Brazil's conclusion that GSM 102 ECGs are unique financing instruments with no parallel at market, because *the IDB, IFC and EBRD are not commercial banks offering market products*. For this same reason, like ExIm Bank fees, IDB, IFC and EBRD fees are distorted by government intervention. Providing additional comparisons between GSM 102 fees and IDB, IFC and EBRD fees is not necessary given the comparison Brazil has already offered to fees charged by U.S.-based ExIm Bank. In that regard, the United States offers no credible evidence to counter the thorough comparative exercise undertaken by Brazil with respect to ExIm Bank products.

ANNEX B-2

EXECUTIVE SUMMARY OF THE REBUTTAL SUBMISSION OF THE UNITED STATES

(Executive summary submitted on 12 February 2007)

1. <u>Preliminary Ruling Requests</u> **– Brazil has failed to rebut the U.S. showing that Brazil's claims relating to GSM 102 guarantees in respect of exports of pig meat and poultry meat are outside the scope of this proceeding.** Brazil concedes that there have never been any findings of WTO inconsistency against the pig meat and poultry meat GSM 102 guarantees, and that there consequently were no DSB recommendations and rulings against these measures with which the United States was obligated to comply. Thus, the claims made by Brazil against these measures are not properly the subject of a compliance proceeding under Article 21.5 of the DSU. Although Brazil contends that "Appellate Body jurisprudence" provides it with the right to "reassert" claims under the Agreement on Agriculture and the SCM Agreement with respect to these measures, Brazil is mistaken. It simply misreads the Appellate Body's report in *EC – Bed Linen (21.5 – India)* and continues to confuse two distinct issues – (a) the scope of a compliance proceeding pursuant to Article 21.5 of the DSU and (b) when a claim against a specific measure or aspect of a measure can be considered to be "finally resolved" for purposes of WTO dispute settlement.

2. – **Brazil has no basis to assert claims against either the marketing loan or counter-cyclical payment programs whether alone or in addition to payments under the programs.** Brazil clarifies in its rebuttal submission that it makes claims against the marketing loan and counter-cyclical payment *programs*, as such, *in addition* to all payments authorized thereunder. Even if so, however, Brazil's claims are outside the scope of this proceeding. <u>First</u>, there is no legal or factual basis for Brazil's argument that "[i]n the circumstances of this dispute, a subsidy 'payment' cannot be divorced from a subsidy 'program'" and the argument is undermined by Brazil's own claims and arguments in the original proceeding. Moreover, contrary to Brazil's assertions, the original panel did not make any finding of WTO-inconsistency against the Step 2, marketing loan, and counter-cyclical payment programs alone or in addition to payments. Consequently, there was also no actionable subsidy-related DSB recommendation with respect to these measures. Brazil's claims on the basis of such a mis-characterized recommendation are not properly within the scope of this compliance proceeding.

3. <u>Second</u>, the measures that Brazil seeks to challenge – marketing loan and counter-cyclical payment programs in addition to payments – are *not* measures taken to comply. Indeed, these measures have not been changed to implement any DSB recommendations and rulings or for any other reason; they remain the same as they were in the original proceeding. Under Article 21.5 of the DSU, claims of consistency with a covered agreement can not be made in respect of measures that are *not* measures taken to comply and that are the same measures as in an original proceeding. For this reason too, Brazil's claims – whether against the marketing loan and counter-cyclical payment programs or the programs in addition to payments thereunder – are not properly within the scope of this proceeding.

4. – **Brazil's claims regarding compliance in past periods remain outside the scope of this proceeding.** Brazil has yet to identify any legitimate textual basis for its claims regarding compliance in past periods. Rather, Brazil continues improperly to conflate Article 7.9 of the SCM Agreement and Article 21.5 of the DSU. Contrary to Brazil's assertions, the former provision does not establish the date for assessing compliance with DSU recommendations and rulings; it simply set the date on

which the complaining Member can seek authorization to take countermeasures "commensurate with the degree and nature of the adverse effects determined to exist," as Brazil alleges. In addition, it is not relevant whether "the assessment [of] whether any proposed countermeasures are commensurate" is "tied to the date on which the implementation period expires." In arguing that this provides a basis for assessing *compliance* as of the date set in Article 7.9 of the SCM Agreement, Brazil confuses the mandate of an arbitrator under Article 22.6 of the DSU with that of a compliance panel under DSU Article 21.5. Neither argument provides a legitimate basis for Brazil's claims regarding compliance in past periods.

5. Export Subsidies **– The United States is not providing export credit guarantees in contravention of Articles 10.1 and 8 of the *Agreement on Agriculture.*** The United States has demonstrated that even before (1) elimination of the GSM-103 program; (2) cessation of the Supplier Credit Guarantee Program ("SCGP"); (3) removal of the highest risk countries from program eligibility and (4) an average fee increase of 46 per cent, premia collected for the GSM-102, GSM-103, and SCGP were more than adequate to cover the long-term operating costs and losses of the programs. Indeed, the current U.S. budget data now reflects that for the cohorts 1992-2005, the applicable total net negative present value amount is **$166,549,780** (*i.e.*, reflecting a 'profit' – excluding administrative costs – to the United States government). Brazil's argument in response – asserting that these results were "specifically created by the United States for purposes of this litigation" – are entirely baseless. Moreover, Brazil's attempts to have the Panel disregard the budget data is inconsistent with the approach taken by the original panel as well as Brazil's positions in the original proceeding. Brazil's own constructed "cash-basis accounting methodology," which Brazil seeks to have the Panel use instead of the budget data provided by the United States, was not accepted by the original panel and is deeply flawed.

6. **– Contrary to Brazil's assertions, the GSM-102 Program is structured and designed to cover long-term operating costs and losses.** First, the size of the cash recoveries in conjunction with the substantial modifications to the export credit guarantee programs belie Brazil's assertion that "the GSM 102 program is not structured or designed to meet long-term operating costs and losses." Contrary to Brazil's assertions, the fact that CCC borrows from the U.S. Treasury in connection with the export credit guarantee programs does *not* mean the programs cannot satisfy the item (j) test. In addition, the fact that there remains a statutory one percent cap on fees under the export credit guarantee programs also does not affect the analysis; CCC has accounted for this fact by eliminating from eligibility **22 countries** with respect to which participation in the program might require fees in excess of the statutory maximum. And, finally, Brazil has no basis to argue that "prudent fiscal management" requires no only imposing the tight exposure limits that CCC employs, but also applying different fees for different banks, as Brazil would prefer.

7. Second, Brazil is incorrect to assert that CCC predicts every year, including for FY 2006 and 2007, that the export credit guarantee programs will incur losses. Brazil assumes (1) the specific experience of the CCC programs in particular are the historical experience used in the calculation of the original subsidy rates and (2) CCC itself provides the principal factors used in the calculation of the original subsidy rates. Both of these assumptions are false. It is the Office of Management and Budget ("OMB") that determines expected loss rates for CCC – and other government agencies – on a government-wide basis. These rates – which are applied to virtually all U.S. agencies providing international credits – are based on assumptions regarding risk and recovery rates involving the highest-risk countries and overstate possible losses in respect of CCC's export credit guarantees programs.

8. **– Whether or not any debt has been rescheduled under the SCGP is irrelevant to whether the United States has "withdrawn" any subsidy under the program.** There are currently no claims "outstanding" under the SCGP. This means that the United States has paid all claims that were payable and is no longer exposed to any further potential liability under the SCGP. Brazil's

argument to the effect that claims may still be outstanding under the program if the United States has rescheduled debt under the program either before or after 1 July 2005 are baseless. They betray a fundamental misunderstanding of the nature of rescheduled debt, which is a *receivable*, pursuant to which CCC expects to *receive – not pay* – money; rescheduled debt is *not* an outstanding *claim*.

9. **– The GSM 102 Program does not confer any benefit under Articles 1 and 3 of the SCM Agreement.** Although Brazil continues to pursue its "claim" under item (j) in the "alternative," it provides no textual basis for doing so. Brazil's approach does not comport with the text of the SCM Agreement or Brazil's own arguments in other disputes that, in the case of measures identified in the Illustrative List, it is the specific provisions of the Illustrative List – and not the general subsidy provisions in Articles 1.1 and 3.1(a) – that govern when the measures may be considered export subsidies. Nonetheless, the United States also shows that GSM 102 export credit guarantees do not confer a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement. This further confirms the fact that item (j) correctly illustrates that GSM 102 export credit guarantees are not export subsidies.

10. Although it purports to make a showing under Article 14(c) of the SCM Agreement, Brazil has made no attempt to make a particularized showing that the overall cost, including fees, of *a loan* guaranteed by the government is less than that the firm receiving the guarantee would pay on a *comparable* commercial loan. Instead, Brazil seeks to advance a flawed "severable 'benefit'" approach that ignores the fundamental fact that costs are distributed among the parties involved. Because costs and potential benefits can both be shared in various ways among all participants in a loan transaction covered by a government guarantee, Article 14(c) focuses on the overall costs of the loan, including the guarantee fees, rather than any single "severable" component of the entire transaction. Brazil's approach is, thus, undermined by the text itself.

11. Unlike Brazil, the United States has provided specific information to demonstrate that sources of financing and guarantees comparable to GSM-102 guarantees are available in the marketplace. Brazil's attempts to discredit the specific, real-world evidence submitted by the United States are entirely unavailing. For example, Brazil attempts to dismiss the numerous examples of commercial products offered by the International Finance Corporation ("IFC"), Inter-American Development Bank ("IDB"), and the European Bank for Reconstruction and Development ("EBRD") that are directly comparable to GSM 102 guarantees. Brazil asserts that, by definition, anything that the IDB, IFC, and EBRD do in the market cannot be commercial and cannot be considered as a benchmark. Once again, Brazil's argument is baseless as a matter of logic and – given the clear evidence of the commercial and profitable nature of these organizations – as a matter of fact.

12. **<u>Actionable Subsidies</u> – Brazil's arguments about the "relatively modest" effects of the elimination of the Step 2 program continue to be unsubstantiated and inconsistent with its earlier positions.** Brazil's fails to substantiate its arguments aimed at minimizing the effects of eliminating the Step 2 program. <u>First</u>, regardless of whether one considers Brazil's "present" or "threat" of serious prejudice claims, there is no merit to Brazil's suggestion that an increase in counter-cyclical payments will offset any positive impacts of terminating the Step 2 program. To the contrary, terminating the Step 2 program *does* result in a decline in marketing loan payments in the few remaining years in which marketing loans are even projected to be paid. Moreover, any increase is counter-cyclical payments is unlikely to take place in the "present" marketing year (MY 2006) and, in future marketing years, it is unlikely to be substantial. This is irrelevant, in any regard, as both marketing loan and counter-cyclical payment programs are scheduled to expire at the end of MY 2007.

13. <u>Second</u>, Brazil continues to argue that the termination of the Step 2 program has had allegedly "relatively modest" *effects* because of the relatively smaller *size* of outlays under the Step 2, marketing loan, and counter-cyclical payment programs. However, Brazil fails to explain why *size* is the

determinative consideration in assessing their *effects*, especially given Brazil's arguments to the contrary to the Appellate Body as well as the *disproportionate* effects that Brazil attempted to attribute to the Step 2 program in the original proceeding.

14. Third, Brazil's new emphasis on the allegedly "modest revenue-enhancing effects" of the Step 2 program is undermined by its own arguments to the original panel that effects on revenue are only one way in which, in Brazil's view, Step 2 payments could have affected world market prices. Brazil argued before that "the *export-enhancing nature* of the Step 2 program" was the other, primary, way in which the Step 2 program affected world marketing prices. Indeed, although Brazil now attempts to downplay its attribution of an "export-enhancing" effect to the Step 2 program, these arguments are simply not credible.

15. Finally, data showing historically low export levels for MY 2006 continue to undermine Brazil's theory of a "relatively modest" impact of eliminating the Step 2 program. Brazil points to the importance of other factors – including the "specific needs of China" – in assessing changes in the world cotton market since MY 2006. However, even taking into consideration the impact of China's demand, U.S. exports appear to be at unusually low levels. Moreover, U.S. *share* of China's imports following termination of the Step 2 program are at unusually low levels. Similarly, the data do not support Brazil's suggestion that the low export levels can be explained by "a temporary surge of U.S. exports in the months just prior to the elimination of the Step 2 subsidy with exporters cleaning out the stocks in their warehouses to take advantage of the Step 2 subsidy."

16. **– Brazil has failed to make a *prima facie* case of "present" serious prejudice within the meaning of Articles 5(c) and 6.3(c) of the SCM Agreement.** As a preliminary matter, the United States notes that the marketing year relevant to Brazil's "present" serious prejudice claims is MY 2006. Where there is reliable data available for MY 2006, or any part thereof, there is no reason why the Panel should not consider that data and Brazil has no basis for suggesting that the data is not relevant.

17. *Brazil has not provided evidence regarding the structure, design, and operation of the marketing loan and counter-cyclical payment programs that supports its claims of significant price suppression:* Brazil has yet to submit any credible evidence confirming the significant production effects from counter-cyclical payments or marketing loan payments that it alleges. Moreover, Brazil has failed to rebut the U.S. evidence showing, with respect to the counter-cyclical payment program, that the recent studies show, at most, minimal production effects. Brazil attempts to discredit the U.S. studies by arguing, *inter alia*, that the studies do not deal specifically with upland cotton production. However, that is not a reason to preclude the Panel from considering the studies as being highly probative. Moreover, Brazil submits *no empirical evidence* of its own relating to upland cotton production that supports it claims. Indeed, the only study that it submits that even deals with counter-cyclical payments is not based on empirical evidence but, instead, was conducted in a computer lab at the University of Wyoming to test the responses of economics students under certain parameters that were necessarily abstracted from actual features of the 2002 Farm Act and imposed a number of limiting assumptions that the authors themselves recognized affected the results of the study.

18. In addition, Brazil fails to rebut the evidence showing that a substantial amount of government payments, including counter-cyclical payments, are "passed-through" to non-operator landowners in the form of higher land rent. Brazil's response confuses the issues and asserts, without basis, that uncertainty about receiving payments precludes capitalization into land values. That argument is inconsistent with the economic literature, Brazil's own arguments regarding U.S. producers' decisions to plant on the expectation of counter-cyclical payments, and the original panel's own findings. Brazil's assertions about the **"relatively minor" effects of decoupled payments on land values are equally unfounded.**

19. Brazil also fails to rebut the acreage data showing that, in fact, *holding upland cotton base acreage has not induced upland cotton production* as Brazil alleges. Brazil's attempts to dismiss these facts as "unimportant" are inexplicable and baseless. In fact, these facts *are* "important" and undermine Brazil's theory of significant production effects, especially Brazil's unfounded assertions regarding producing for the possibility of base updating.

20. With respect to marketing loan payments, Brazil fails to demonstrate that – taking into account the particular structure and design of the marketing loan program, and the way that it operates under the current market conditions – payments thereunder *are* in fact causing production effects that are so significant as to be suppressing the world market price for cotton. In particular, Brazil fails to analyze properly the planting decisions made by U.S. producers in light of the market conditions and considerations that they *actually* faced at the time of planting, even as Brazil concedes that this is the appropriate inquiry. Moreover, while Brazil attempts to discredit the U.S. analysis of producers' planting decisions, it has provided no legitimate basis for its arguments.

21. <u>*Brazil fails to provide any credible evidence showing that U.S. producers and exporters do not respond to market signals*</u>*:* The empirical evidence fatally undermines Brazil's theory that marketing loan and counter-cyclical payments insulate U.S. producers and exporters from market signals. Brazil has yet to provide any credible answer to the fundamental question in this regard: *if U.S. producers continue to plant and produce, and U.S. exporters continue to export, in circumstances where "any rational non-subsidized producer" would have "reduced plantings, production, and exports,"* <u>*why has U.S. share of world production and world exports not increased over the life of the FSRI Act of 2002*</u>*?* Rather, Brazil attempts to confuse the issues by suggesting that the determinative question is whether marketing loan and counter-cyclical payments provide *income* support to U.S. producers. It is not; in fact, there is no WTO obligation to abstain from providing such support. The question is whether a subsidy causes one or more of the four types of "effects" reflected in Article 6.3 of the SCM Agreement. Brazil has submitted *no* empirical evidence that the marketing loan and counter-cyclical payments causes these effects and, indeed, the empirical evidence that the United States has submitted flatly contradicts Brazil's arguments in this regard. Brazil's attempts to rebut that evidence – for example, by asserting that the stability in U.S. share of world production and exports are themselves evidence of significant price suppression – are entirely unfounded.

22. In addition, Brazil's attempts to demonstrate an alleged absence of a "link" between "prices, on the one hand, and [U.S.] planted acreage, production, and exports, on the other hand" do not withstand scrutiny. Every comparison that Brazil has made in this regard has been fundamentally flawed, including its latest attempt to plot U.S. *planted* acreage against foreign *harvested* acreage and upland cotton futures; an approach that (a) improperly compares planted and harvested acreage, (b) ignores the fact that producers look at more than upland cotton futures prices in determining what to plant, and (c) attempts to capitalize on differences that appear to exist solely because of the particular graph utilized. Brazil's attempts to compare *changes* in U.S. *planted acreage*, changes in foreign *harvested* acreage, and *changes* in the futures prices for upland cotton are equally flawed. What that comparison shows is that *neither* U.S. nor foreign harvested acreage moves closely with futures prices of cotton *alone*. Nonetheless, even if the comparison were valid (and it is not), it would show that, where changes in U.S. and foreign area diverge, U.S. harvested acreage tends to react *more conservatively* than foreign acreage to increasing prices.

23. Finally, Brazil continues to assert incorrectly that *increases* in the absolute levels of U.S. production over the period from MY 2002-2005 were the effect of the marketing loan and counter-cyclical payment programs. Brazil's arguments in this regard are not even internally consistent, let alone supported by the facts.

24. <u>*Brazil Fails to Show Any "Discernible Temporal Coincidence"*</u>*:* Contrary to its assertions, Brazil had not "reinforce[d] the original panel's finding . . . of a discernible temporal coincidence of suppressed world market prices and the price-contingent U.S. subsidies." To the contrary, the factors considered by the original panel do *not* support finding of a "discernible temporal coincidence" between the marketing loan and counter-cyclical payment programs and any "present" significant price suppression. Brazil's new assertion that it should be excused from making even the minimum showing of a "discernible temporal coincidence" as conducted by the original panel would effectively eviscerate the balance of rights and obligations struck in Articles 5(c) and 6.3(c) of the SCM Agreement and the requirement that a complaining party make a *prima facie* case of breach.

25. <u>*Brazil has not shown that U.S. producers would switch to other crops or exit cotton farming without marketing loan and counter-cyclical payments*</u>*:* There is no basis for Brazil's argument that marketing loan and counter-cyclical payments are necessary to fill an alleged "gap" between costs of production and market revenue, without which U.S. producers would cease farming cotton. <u>First</u>, the economic literature makes clear that producers make year-to-year planting decisions with reference primarily to *variable* costs of production (among other factors) and that *total* costs (among other factors) are relevant with respect to longer-term decisions, such as whether to exit the cotton sector. <u>Second</u>, the evidence shows that U.S. producers *covered their variable costs* in every year that the FSRI Act has been in effect and that, therefore, it was economically rational for U.S. producers to have produced upland cotton in these years. Brazil efforts to inflate variable costs by including land, labor, and capital recovery costs as variable costs are not supported by the economic literature. Further, Brazil has not shown that farmers actually take these costs – for example, an "imputed cost of unpaid labor" – into account in each year in deciding between planting cotton or some other crop or putting the land to some other use.

26. <u>Third</u>, Brazil's arguments against adjusting the seed cotton (i.e., cotton lint plus cottonseed) costs and revenues to isolate the revenue and costs for cotton lint (the product that is at issue under Brazil claims) are baseless. Contrary to Brazil's assertions, the evidence shows the common practice in the United States of paying ginning costs out of the proceeds gained by the gin from sale of the cottonseed separated out in the ginning process. This supports the U.S. approach of excluding both ginning costs and revenue from sale of cottonseed. However, even using a more conservative methodology that (a) excludes ginning costs only up to the amount of cottonseed revenue; and (b) including hired labor as a variable cost shows that U.S. producers have not only made their variable costs in all years but their total costs in many years as well.

27. <u>Fourth</u>, with respect to longer-term decisions, such as whether to continue or exit upland cotton farming, the United States has explained that the total cost of producing upland cotton is not the *sole* consideration. As the economic literature confirms, whole-farm costs and revenues – including off-farm revenue and revenue from other sources – are also important considerations in making those kinds of decisions. Brazil's attempts to show that U.S. producers would have exited upland cotton production in the long-term solely on the basis of a comparison of costs and revenues for cotton are, thus, not sound. To date, Brazil has not submitted any literature, study, report, or empirical evidence that contradicts the evidence submitted by the United States regarding the consideration of whole-farm costs and revenues. Nor has Brazil provided any evidence taking into account whole-farm costs and revenues that show that, absent the marketing loan and counter-cyclical payment program, U.S. upland cotton producers would have exited upland cotton farming.

28. <u>*Neither Brazil's New Modeling Exercise Nor the Studies It Selectively and Misleadingly Cites Supports Its Claim of Significant Price Suppression*</u>*:* Brazil's new econometric model – on which most of Brazil's arguments critically depend – substantially overstates any possible effects on world market prices from the removal of the marketing loan and counter-cyclical payment programs. It is based on a series of untenable economic assumptions that are <u>*not*</u> consistent with those used by FAPRI or USDA economists and were not even used *by Brazil* in its own analysis before the original

panel. When certain basic assumptions in the model are changed to *actually* reflect FAPRI and other well-established parameters, the effects predicted by Brazil's model decline sharply.

29. Brazil now attempts to justify its novel modeling assumptions by criticizing the FAPRI-based model – and assumptions – that it used in the original proceeding as being "unnecessarily complicated and cumbersome" and "not directly appropriate to the issue at hand." These assertions directly contradict the arguments made by Brazil to the original panel. Moreover, their grossly inflated nature is evident when one considers that Brazil has – by using this new model – increased the asserted price effects *almost three-fold*. There is no reason for this other than the use by Brazil of unreasonable, unsupported modeling assumptions for purposes of this proceeding.

30. Brazil's efforts to justify its flawed modeling results by comparing them to the results of studies examining completely different factual scenarios are logically unsound. In fact, it is evidence of the *unreasonableness* of Brazil's approach that Brazil ascribes to marketing loan and counter-cyclical payments, alone, similar (or in some cases, *greater*) price effects than (a) a 2006 World Bank study estimates for the elimination of *all* subsidies and tariffs across *all* countries; (b) a 2004 study by the Overseas Development Institute ("ODI") estimates for the elimination of domestic supports in China, Greece, Spain, and the United States; (c) and a study by FAO estimates for the elimination of all domestic support in all countries. Even less persuasive is Brazil's attempt to place its results "in the mid-range" of the studies surveyed by the FAO, World Bank, and International Food Policy Research Institute ("IFPRI"), all of which examine the effects of a much different "basket" of measures that those examined by the Panel here. Finally, Brazil does not undermine recent studies showing that the marketing loan and counter-cyclical payment programs likely only have *minimal effects* on world market price.

31. *Brazil Has Not Ensured that the Price Effects Of Other Factors Are Not Attributed to the Marketing Loan and Counter-cyclical Payment Programs:* Brazil fails to undertake any meaningful assessment of the world upland cotton market, of actual world market prices, or of the factors that are observed to be affecting U.S. and foreign supply and demand and, ultimately, world market prices. The Appellate Body underscored the importance of such an assessment in this dispute, explaining that in order to prove a claim under Article 5(c) and 6.3(c) of the SCM Agreement, "it is necessary to ensure that the effects of other factors on prices are not improperly attributed to the challenged subsidies." *Upland Cotton (AB)*, para. 437. Brazil has not carried its burden in this regard.

32. For example, although China is the world's *largest producer* of upland cotton, the world's *largest consumer* of upland cotton, and the world's *largest importer* of upland cotton, Brazil does not assess and distinguish any impacts of China's trade on world market prices. Instead, Brazil seeks to mischaracterize the U.S. arguments as being against the original panel's finding that the United States exerts a substantial proportional influence on the world market price of upland cotton. Moreover, Brazil argues that the United States is confusing Brazil's claims of price *suppression* with claims of price *depression*. Neither argument is valid; the former is simply erroneous and the latter overlooks the fact that the market reports and data that the United States submits are relevant to price *suppression*, not price *depression*. By contrast, Brazil has submitted no empirical evidence itself that confirms its claims of price suppression. And Brazil's attempts to dismiss the evidence showing the importance of China's trade on world market prices are without merit.

33. *Brazil Fails To Provide Any Evidence or Arguments Regarding "Significant" Price Suppression In Its Rebuttal Submission:* The United States explained in its first written submission that Brazil has not demonstrated either through empirical evidence, or through its modeling exercise, that the marketing loan and counter-cyclical payment programs have had any appreciable impacts on price in MY 2005, let alone caused any "significant" price suppression within the meaning of Article 6.3(c) of the SCM Agreement. Brazil does not even address the question of "significance" in

its rebuttal submission and, thus, fails to prove a critical element of its claims of "significant" price suppression under Articles 5(c) and 6.3(c) of the SCM Agreement.

34. **– Brazil has failed to make a *prima facie* case of breach under Articles 5(c) and 6.3(d) of the SCM Agreement.** Brazil had not made a *prima facie* case that the marketing loan and counter-cyclical payment programs breach Articles 5(c) and 6.3(d) of the SCM Agreement. First, Brazil provides no legitimate empirical evidence to support its assertion that the slight increase in the U.S. share of the world market in MY 2005 over the average for MY 2002-2004 was "the effect" of the marketing loan and counter-cyclical payment programs. Moreover, Brazil analysis is premised on the incorrect assumption that Article 6.3(d) is concerned with absolute market share and whether or not, in any given year, a Member's market share would have been lower if subsidies were removed. It is not; by its terms, Article 6.3(d) applies only in those situations where there is an increase from the previous three-year average and it is this *increase* over time that is "the effect" of subsidies. Thus, Brazil's argument is entirely off the mark.

35. Second, Brazil's arguments assume that Article 6.3(d) requires a showing of an *upward trend* in market share. However, Article 6.3(d) requires a showing that "this increase" – *i.e.*, "the increase in the world market share of the subsidizing Member . . . as compared to the average share it had during the previous period of three years" – "follows a consistent trend over a period when subsidies have been granted." Brazil does not even provide relevant data in this regard, let alone make the required demonstration. Nor could it; there simply is no such "consistent trend." Brazil has, thus, failed even to submit a proper analysis, let alone established a *prima facie* case of breach under Articles 5(c) and 6.3(d) of the SCM Agreement.

36. **– Brazil has failed to make a *prima facie* case of threat of serious prejudice under Articles 5(c) and 6.3(c) of the SCM Agreement.** Brazil's claims of "threat" of serious prejudice fail because they are based on a legally erroneous standard and are factually unsubstantiated. First, there is no basis for Brazil's argument that "the precedent interpreting the terms 'threat' and 'threaten' suggests that the appropriate standard of threat in Part III [of the SCM Agreement] is one in which there is a significant likelihood, based on the nature of subsidies and particular conditions of competition, that serious prejudice will occur in the future." This "significant likelihood" standard is not found in the text of the SCM Agreement. Moreover, even leaving aside that there is no basis to attempt to interpret a treaty in accordance with "precedent" rather than "in accordance with customary rules of interpretation of public international law," Brazil does not in fact identify any "precedent" that "suggests" that the appropriate standard for "threat" of serious prejudice is "a significant likelihood." As Brazil's claims are based on an erroneous legal standard, Brazil fails to make a *prima facie* case of threat of serious prejudice within the meaning of Article 5(c) and footnote 13 of the SCM Agreement.

37. Moreover, Brazil's threat claims are also factually unfounded. For example, given the prices that are expected to prevail in MY 2007 (well above 52 cents/lb), it is unlikely that marketing loans will have any significant effects on planting, production, exports, or world market prices in MY 2007. Indeed, recent estimates project that any marketing loan payments are likely to be small in MY 2007 and not even paid out in MY 2008. Moreover, counter-cyclical payments are likely to be paid in near-fixed sums at least through MY 2007 (i.e., meaning that they are likely to behave much like fixed, direct payments which have been found not to cause any significant price suppression). Projections for MY 2007 U.S. plantings, production, and exports – all of which show declines – also undermine Brazil's claims of "threat of serious prejudice." Moreover, cost data for future marketing years show that U.S. producers will likely cover their variable, or operating, costs as well as a large share of total costs in MY 2007.

ANNEX B-3

EXECUTIVE SUMMARY OF BRAZIL'S SUBMISSION REGARDING U.S. REQUEST FOR PRELIMINARY RULING

(Executive summary submitted on 23 January 2007)

1. Brazil addresses the four requests for preliminary ruling included in the United States' First Written Submission and asks that the compliance Panel reject each of the United States' requests.

1. USE OF GSM 102 TO SUPPORT EXPORTS OF PIG MEAT AND POULTRY MEAT ARE PROPERLY BEFORE THE COMPLIANCE PANEL

2. In this dispute, Brazil claims that the United States has applied General Sales Manager 102 export credit guarantees ("ECGs") in a manner that circumvents U.S. export subsidy commitments with respect to "unscheduled" products and three "scheduled" products – rice, pig meat and poultry meat.

3. According to the United States, Brazil cannot assert claims about ECGs for pig and poultry meat in an Article 21.5 proceeding, allegedly because "the Appellate Body made no findings against those guarantees [for exports of pig meat and poultry meat] and the DSB thus issued no rulings and recommendations addressed to them." The United States concludes that Brazil's claims are outside the scope of these proceedings.

4. The United States advances an incorrect interpretation of Article 21.5 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"). The scope of Article 21.5 proceedings is not limited in this regard by the scope of the original proceedings in this dispute. As affirmed by the Appellate Body in *EC – Bed Linen (21.5)*, "an *unappealed* finding included in a panel report that is *adopted* by the DSB must be treated as a *final resolution* to a dispute between the parties in respect of the *particular* claim and the *specific* component of a measure that is the subject of that claim."[1] Brazil successfully appealed the original panel's finding that the United States had not circumvented its export subsidy commitments with respect to ECG support for exports of pig meat and poultry meat, but the Appellate Body was unable to complete the analysis. Thus, unlike in *EC – Bed Linen (21.5)*, there has been no "final resolution" to the question whether the United States circumvents its export subsidy commitments with respect to ECGs for pig meat and poultry meat. The scope of the original proceedings does not, therefore, limit the scope of the Article 21.5 proceedings in this respect. Hence, Brazil's claim concerning the consistency with Article 10.1 of the ECG programs with respect to pig meat and poultry meat is properly within the scope of these Article 21.5 proceedings.

5. Accordingly, Brazil requests that the compliance Panel reject the United States' request for preliminary ruling.

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[1] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 93 (emphasis in original). *See also* Appellate Body Report, *U.S. – Softwood Lumber VI (21.5)*, para. 102 (footnote 150).

2. THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENT PROGRAMS ARE PART OF THE U.S. "MEASURE TAKEN TO COMPLY"

6. The United States requests a preliminary ruling that the marketing loan and counter-cyclical payment programs are not "measures taken to comply," within the meaning of Article 21.5 of the DSU.

7. With its request for preliminary ruling, the United States appears to suggest that, since it chose to implement the recommendations and rulings of the Dispute Settlement Body ("DSB") by solely removing the Step 2 program, these Article 21.5 proceedings can only address the effects of the removal of the Step 2 program, without regard to the other two measures that formed the "basket of measures" to which the findings, conclusions and recommendations of the original panel relate. The U.S. position ignores the context of the original panel's rulings, as well as the text of Article 21.5.

8. First, the U.S. argument ignores that the findings, conclusions and recommendations of the original panel apply to a "basket of measures."[2] U.S. statements at the time the Step 2 program was repealed indicate that the repeal of the Step 2 program was intended to comply with the adverse effects-related recommendations and rulings of the DSB, which apply to a "basket of measures."

9. Second, by repealing the Step 2 program, the United States changed the "basket of measures" to which the adverse effects-related recommendations and rulings of the DSB apply. The question before the compliance Panel is whether this *new* basket of mandatory and price-contingent measures, which constitutes the "measures taken to comply," is "consistent with the covered agreements."

10. Brazil notes that Australia, Canada, Chad, China, the European Communities, New Zealand and Japan disagree with the U.S. arguments that its failure to change a non-compliant measure means that such a measure should fall outside the scope of proceedings under Article 21.5 of the DSU and request that the compliance Panel reject the U.S. request for preliminary ruling.

11. Accordingly, Brazil requests that the compliance Panel reject the United States' request for preliminary ruling.

3. THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENT PROGRAMS ARE PROPERLY WITHIN THE SCOPE OF THESE ARTICLE 21.5 PROCEEDINGS

12. The United States argues that Brazil's claims in these Article 21.5 proceedings concerning the serious prejudice and threat of serious prejudice caused by the marketing loan and counter-cyclical programs are outside the scope of these proceedings, because the original panel "either rejected or declined to address" claims against those programs.

13. *First*, the United States argues that Brazil raises improperly an "as such" claim in these Article 21.5 proceedings. Yet, contrary to the US's assertions, Brazil does not raise a claim against U.S. marketing loan and counter-cyclical payment programs "as such." Rather, Brazil challenges these programs inasmuch as they cause adverse effects, within the meaning of Articles 5 and 6 of the *Agreement on Subsidies and Countervailing Measures* ("*SCM Agreement*"). Indeed, Brazil makes no distinction between the serious prejudice caused by the statutory and regulatory framework of the FSRI Act of 2002 and the serious prejudice caused by the mandatory and price-contingent payments flowing from that statutory and regulatory framework.

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[2] Panel Report, *U.S. – Upland Cotton*, paras. 7.1502 and 7.1503.

14. In the circumstances of this dispute, a subsidy "payment" cannot be divorced from a subsidy "program." The original panel made it very clear that its "present" serious prejudice finding *pertains* to *both* the FSRI Act of 2002 subsidy programs and the payments mandated by those programs.

15. The United Stated did not appeal this particular element of the original panel's report, which was, therefore, adopted by the DSB. Consequently, the United States "is obliged to take action concerning its present statutory and regulatory framework as a result of [the original panel's] 'present' serious prejudice finding."[3] The U.S. arguments regarding the "as such" versus "as applied" distinction reflect a fundamental misconception concerning the nature of the obligations Articles 5, 6 and 7.8 of the *SCM Agreement*, and the DSB recommendations and rulings in this dispute.

16. *Second*, application of WTO jurisprudence regarding the limits imposed on the scope of Article 21.5 proceedings by the scope of the original proceedings[4] makes it clear that Brazil's claims against the U.S. marketing loan and counter-cyclical payment programs, and the payments flowing from such programs, are properly before this compliance Panel.

17. Brazil's claims regarding the adverse effects flowing from both the programs and payments mandated thereunder were identified in Brazil's request for establishment of this compliance Panel. Brazil's claims involve U.S. measures "taken to comply" with the recommendations and rulings of the DSB – specifically, the new "basket of measures" providing for mandatory and price-contingent domestic support for upland cotton created by the repeal of the Step 2 program. Moreover, as demonstrated in more detail below, the original panel did not reject, as the United States argues, Brazil's claims that the marketing loan and counter-cyclical payment programs, or the mandatory and price-contingent payments made thereunder, cause serious prejudice or a threat thereof.

18. Brazil's claims concerning the marketing loan and counter-cyclical payment programs and the payments flowing from such programs in these Article 21.5 proceedings, therefore, fall squarely within the limits set by panels and the Appellate Body in their jurisprudence.

19. Furthermore, as clarified by the original panel, its "'present' serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002 [and that] the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice finding." Indeed, the original panel made findings that explained that its present serious prejudice conclusions "pertain" to both "measures in force" and "subsidies paid." This is consistent with the original panel's identification of both payments and the statutory and regulatory framework providing for these payments as the "measures at issue."

20. Numerous other statements by the original panel confirm this. For example, the original panel recognized that price-contingent *payments* are inextricably linked to the mandatory statutory and regulatory framework, *i.e.*, the *programs*, providing for them. In discussing the nature of the subsidies at issue, the original panel referred numerous times to the statutory and regulatory framework providing for these payments.

21. Additionally, the original panel repeatedly stated that its "present" serious prejudice finding were premised upon effects generated from *both* the FSRI Act of 2002 *and* the payments flowing from the FSRI Act of 2002. Its statements show that it was convinced that the United States could only comply with its Article 7.8 obligations by changing the mandatory and price contingent "basket of measures" of the FSRI Act of 2002.

[3] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.
[4] *See US – Softwood Lumber VI (21.5)* and *Chile – Price Band Systems (21.5).*

22. The original panel also left no doubt that it considered the "basket of measures" alleged by Brazil to cause a *threat* of serious prejudice during MY 2003-2007 to overlap with the same "basket of measures" that the United States was obliged to change as part of its obligation, pursuant to Article 7.8, to comply with the original panel's *present* serious prejudice findings.

23. For these reasons, the original panel did not find it "necessary or appropriate" to rule on Brazil's "threat" claims. This finding did not constitute a rejection of those claims. The original panel's statements regarding the United States' *obligation* to "make changes to its statutory and regulatory framework" were a direct response to a request by Brazil to address future adverse effects flowing from the FSRI Act of 2002.

24. Finally, the original panel did not reject Brazil's *per se* claim. Indeed, it exercised judicial economy over that claim. In doing so, the original panel cross-referenced to Sections G and H of its report making it clear that no *additional* findings were necessary.

25. In light of the foregoing, Brazil requests that the compliance Panel reject the United States' request for preliminary ruling.

4. THE COMPLIANCE PANEL IS NOT BARRED FROM MAKING FINDINGS WITH RESPECT TO THE U.S. FAILURE TO IMPLEMENT BETWEEN 21 SEPTEMBER 2005 AND 31 JULY 2006

26. The United States asserts, first, that Brazil cannot raise a claim, under Article 21.5 of the DSU, if there is no disagreement between the parties concerning the existence of measures taken to comply. In doing so, the United States seems to acknowledge the absence of measures to comply between the end of the implementation period on 21 September 2005 and 31 July 2006. Brazil thus requests the compliance Panel to make a finding to that effect.

27. Second, the United States asserts that the compliance Panel is barred, by Article 21.5 of the DSU, from making findings on a situation of non-compliance by the United States between 21 September 2005 and 31 July 2006.[5] The United States errs. Brazil has the right to challenge the "existence" and "consistency" of "measures taken to comply", in accordance with Articles 7.8 and 7.9 of the *SCM Agreement*. A finding that the United States failed to implement in a timely manner will be relevant to the resolution of this dispute.

28. Should Brazil prevail in the adverse effects-related portion of this dispute, the quantification of any countermeasures it seeks will be assessed by an arbitrator as of the date the United States was required to "remove the adverse effects of the subsidy or withdraw the subsidy." Arbitrators refer to "the date on which the implementation period expired, as the date on which to assess whether the proposed suspensions of concessions or other obligations were equivalent to the level of nullification or impairment or constitute appropriate countermeasures."[6]

29. Accordingly, Brazil's right to pursue the United States' failure to remove the adverse effects or withdraw the subsidy, and the assessment whether any proposed countermeasures are commensurate, *are tied to the date on which the implementation period expires*. That the United States, on 1 August 2006, took measures to comply is relevant before this compliance Panel solely in connection with Brazil's claims that these measures result in inconsistency with Articles 5 and 6 of the *SCM Agreement*.

[5] U.S. First Written Submission, paras. 51-56.
[6] Arbitrator's Report, *U.S. – FSC*, paras. 2.14(a) (and footnote 25), 2.15.

30. Brazil notes that Australia similarly points out to the impact the U.S. interpretation would have on Members' rights under Article 7.9 of the *SCM Agreement* and Article 22 of the DSU.

31. Brazil therefore requests that the compliance Panel reject the United States' request for preliminary ruling.

5. CONCLUSION

For the reasons set forth in Sections 1 to 4 above, Brazil requests that the compliance Panel reject all four U.S. requests for preliminary rulings.

ANNEX C

ORAL STATEMENTS OF PARTIES AND THIRD PARTIES AT THE MEETING WITH THE PANEL

ANNEX C-1

EXECUTIVE SUMMARY OF THE OPENING STATEMENT OF BRAZIL

(27 February 2007)

1. Brazil's "oral statement" addresses the following issues. First, Brazil deals with preliminary rulings arguments. Second, Brazil highlights key aspects of Brazil's present serious prejudice claims and responds to selected arguments raised by the United States in its Rebuttal Submission. Third, Brazil reiterates its claims with respect to export credit guarantees ("ECGs") and rebuts the United States' principal defenses.

1. PRELIMINARY RULINGS ARGUMENT

2. Brazil provided extensive answers to the Panel's questions regarding the preliminary ruling requests of the United States. In considering these arguments, Brazil asks the Panel to consider the following questions. When the original panel issued its report, did it intend to leave Brazil with <u>no implementation rights</u> for serious prejudice caused by mandatory and price-contingent marketing loan and Counter-Cyclical Payment ("CCP") program payments made after marketing year (MY) 2002? Further, did the original panel intend that the United States would have <u>no obligation</u> to take appropriate steps under Article 7.8 of the *SCM Agreement* concerning its <u>statutory and regulatory framework</u> mandating price-contingent marketing loan and CCP subsidies?

3. The original panel expressed very clearly the U.S. obligation to take steps to limit and control marketing loan and CCP subsidies made after 31 July 2003. In addressing Brazil's arguments about the mandated future marketing loan and CCP subsidies made during MY 2003 and to be made beyond, the original panel found that "[b]ecause the Panel's 'present' serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002, the United States is obligated to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice findings." This finding provided considerable assurance to Brazil that the United States was required to significantly change and transform the Farm Security and Rural Investment Act of 2002, the Farm Bill.

4. The United States argument that General Sales Manager ("GSM") 102 ECGs for pig meat and poultry meat are not properly within the scope of these Article 21.5 proceedings confounds Brazil's claims and the measure that is the subject of those claims. Brazil's claims concerning these two "scheduled" commodities are product-specific, as they must be under the *Agreement on Agriculture*. The measure subject to those claims is indeed the United States' "measure taken to comply" – the GSM 102 program "in its totality," as amended by the modified GSM 102 fee schedule. As we demonstrate in our answers to the Panel's questions, neither the amended GSM 102 program in its totality, nor the individual amendments, set out terms or conditions that differ as between any eligible products. Brazil's claims are product-specific, but the U.S. "measure taken to comply" is not.

2. PRESENT SERIOUS PREJUDICE CLAIMS

5. Brazil initiated this proceeding due to the failure of the United States to withdraw the subsidies or to take appropriate steps under Article 7.8 of the *SCM Agreement* to remove the adverse effects of the subsidies, in a timely and complete fashion, pursuant to the recommendations and rulings of the Dispute Settlement Body ("DSB") in this dispute. While Brazil raises four claims in

this proceeding, the focus of this Oral Statement is Brazil's claims of present serious prejudice from the U.S. marketing loan and CCP subsidies.

Cross-Cutting Serious Prejudice Related Arguments

6. Initially, Brazil addresses a number of cross-cutting arguments. First, the appropriate reference period to assess the effects of marketing loan and counter-cyclical payments is MY 2005, the last recent marketing year for which essentially complete data exists. However, it is appropriate for the Panel to assess, where credible and reliable, evidence concerning time periods *after* 31 July 2006.

7. Second, this Panel should follow the findings of the original panel. Brazil fully agrees with the United States that the original panel's findings "are taken as a given for purposes of this Article 21.5 proceeding." The Panel should, therefore, reject the U.S. efforts to have it dismiss practically all of the original panel's findings as irrelevant because allegedly all of its findings relate only to a basket of three measures – marketing loan, CCP and Step 2 subsidies.

8. Third, as every other panel assessing a serious prejudice claim, this Panel must necessarily conduct a counterfactual "but for" analysis. This approach requires it to assess what production, exports, and world prices would be in a world in which U.S. marketing loan and CCP subsidies did *not* exist.

The Nature, Magnitude and Effects of Marketing Loan Subsidies

9. The largest and most trade-distorting subsidy at issue in this dispute is the marketing loan subsidy. The original panel found as follows: "we have no doubt that the [marketing loan] payments stimulate production and exports and result in lower world market prices than would prevail in their absence." The United States now asks this Panel to find that since the adoption of the panel's marketing loan findings by the DSB on 21 March 2005, the nature of marketing loan subsidies has totally changed. However, both the available data and testimony of cotton producers and their representatives shows that marketing loans are crucial for the continued production of cotton. Further, marketing loan payments in MY 2005 were 29 percent *larger* than in MY 2002.

The Nature, Magnitude and Effects of CCP Subsidies

10. CCP subsidies play a similarly crucial role in U.S. cotton producers' ability to grow cotton profitably. According to data produced by the United States for MY 2005, 95 percent of U.S. cotton acreage was planted on farms holding cotton base. These farms receive large amounts of CCP subsidies. These facts alone demonstrate the "strongly positive relationship" between receipt of CCP subsidies and the continued production of cotton. CCP subsidies have production, export and price effects, as they restrict planting flexibility of farmers. They reduce the risk associated with producing the base crop, in this case cotton. CCP subsidies also increase the ability of farmers to invest in production-enhancing equipment. In general, they smooth the revenue flow to farmers and ease access to credit.

11. Representatives of the National Cotton Council ("NCC") of America testified to the U.S. Congress that "during the past three years, many cotton farmers have avoided bankruptcy only because Congress has authorized emergency relief to supplement the FAIR Act's inadequate fixed payments." This statement offers a number of valuable insights also for CCPs. As the original panel found, "United States upland cotton producers rely on … subsidies to cover their cost of production." Second, contrary to U.S. arguments, U.S. producers could not perceive direct payments ("fixed payments") and CCP subsidies as fully capitalized into land values.

Combined Effects of Marketing Loan and CCP Subsidies Result in Increased U.S. Supply of Cotton

12. But for U.S. price-contingent cotton subsidies, the majority of cotton farms would incur huge losses nearly every year. Faced with the prospect of such losses, many farmers would cease producing cotton. Neither the U.S. criticisms of Brazil's cost of production analysis, nor the new factual information provided by the United States, detracts from the core reality that U.S. cotton farming is unprofitable without subsidies.

13. The key question in any business is whether market returns exceed costs and generate sufficient profit. While a business with reserves may sustain losses in some years, even the United States recognizes that "in the long run, producers will have to cover asset and overhead costs, as well as variable costs." Data from USDA indicates that cotton farmers lost an average of $837 for each acre planted to cotton in the past seven years (MY 1999-2005). In only one of these years – MY 2003 – did farmers' market returns exceed production costs. Based on the total amount of acres planted to cotton, the U.S. cotton industry lost $12.4 billion during the past seven years. Yet, over the same period, marketing loan and CCP subsidies provided cotton farmers with price-contingent subsidies amounting to $13.5 billion.

14. The United States claims that Brazil "fails to analyze properly the planting decisions made by U.S. producers in light of market conditions and considerations they *actually* faced at the time of planting." In response, Brazil compared the net revenue (or loss) that a typical farmer holding cotton base expected in the spring of 2005 from growing an acre of cotton, or two common substitute crops, soybeans and corn. The analysis demonstrates that subsidized U.S. cotton farmers did *not* have an incentive to switch from cotton to corn or soybean production. Rather, they expected that cotton marketing loan and cotton CCP payments linked to the cotton base acre at issue would allow them, at a minimum, to break even. Had cotton marketing loan and CCP subsides not existed in MY 2005, upland cotton farmers would have had every incentive to switch to the production of other crops, for which marketing loan subsidies would still be available, to cut its losses.

15. The fact that U.S. marketing loan and CCP subsidies "numb" U.S. cotton farmers' responses to market price signals is also demonstrated by more recent evidence. In February 2007, the NCC announced that U.S. cotton farmers intend to plant 12.8 million acres in MY 2007, or 14 percent *less* than in MY 2006, largely because expected prices for corn are the highest on record. The evidence shows that farmers expect to incur large losses from growing cotton in MY 2007 if they had to consider solely cotton market revenue. By contrast, farmers can expect to earn a profit from growing both soybeans and corn, <u>even without considering U.S. subsidies</u>. Based on these considerations alone, it is remarkable that the NCC predicts that *only* 14 percent of cotton acreage shifts out of growing cotton.

16. Examining actual total costs and returns in MY 2002-2006 demonstrates that only U.S. subsidies made growing cotton economically rational, and very profitable. Again, price-contingent cotton marketing loan and CCP subsidies are the main reason for cotton farmers achieving profitability. The marketing loan subsidy alone almost entirely erased losses that cotton farmers would have incurred based solely on market revenue. It also almost equalized the returns from growing cotton, corn or soybeans. Cotton direct and CCP subsidies then turned growing cotton into a very profitable business.

17. Brazil recalls that even if U.S. cotton farmers expected prices to be above the Adjusted World Price at the time of planting, they "were also aware that if actual prices were ultimately lower, they would be 'insulated' by government support, including not only marketing loan program payments but also counter-cyclical payments, which were based on a target price of 72.4 cents per pound." This is exactly what happened in MY 2004. Futures prices during the planted period indicated high prices at the time of harvest. But soon after planting, prices began to plunge far below the loan rate.

18. Finally, the United States claims that Brazil has failed to show that the effects of marketing loan and CCP subsidies are to *increase* U.S. acreage, *increase* U.S. production, and *increase* the U.S. share of world exports and production. This argument erroneously assumes that there was a recent marketing year, month, or even day without effects from the U.S. subsidies. Such a time period does not exist. Given the original panel's findings regarding the structure, design and operation of the mandatory and price-contingent subsidies in the FSRI Act of 2002, it is sufficient for Brazil to show that those subsidies have sustained and maintained high levels of acreage, production and exports of U.S. cotton that would otherwise be uneconomical.

Statement of Professor Daniel Sumner

19. Professor Sumner provided the Panel with a straightforward and robust model appropriately tailored to the questions before this Panel. The parameters used fit specifically the market and policy setting for cotton and the question that this Panel is tasked to assess – the impacts on cotton market prices, quantities and exports of removing very large cotton subsidies. The United States has raised many complications, yet each of its objections fades away upon scrutiny. The model provided to the Panel and the economic reasoning that guides its application to the issues of U.S. cotton subsidies are sound. The results provided are sound and directly useful for this case.

20. The analysis discusses why the CCP affects acreage decisions of cotton farmers. These payments affect cotton production because they are large, they are tied to the cotton price, they restrict what can be grown, and they are tied to cotton production through expectations about future base updates. The importance and relevance of these arguments are reinforced by the evidence that has accumulated since 2003. It is instructive to note that in its reparameterization of the model by the United States, it abandons its previous claim that the CCP is completely decoupled from production.

21. The basic set of equations was adapted from a research report published by the Cato Institute. While built upon the basic algebraic foundation published as an appendix in my 2005 study, the cotton model used by Professor Sumner for this dispute involves considerable elaboration from the Cato publication.

Production and Export Effects Cause Significant Price Suppression in the World Market and an Increase in the U.S. World Market Share

22. Brazil has demonstrated that excess U.S. production causes significant price suppression in the world market for cotton. Evidence supporting this assertion includes the fact that Brazilian and U.S. cotton is a fungible and widely traded commodity and that "the United States exerts a substantial proportionate influence in the world market for upland cotton." As in MY 2002, the United States accounts for about 20 percent of world production and 40 percent of world exports. Price suppression in the world cotton market today continues to be linked to the U.S. position as the world's largest exporter by far.

23. Furthermore, the evidence demonstrates that the price effects of the U.S. marketing loan and CCP subsidies are "significant." Professor Sumner finding of a 9-11 percent price effect in the world market for cotton in MY 2005 is supported by the academic literature.

24. The price effects from marketing loan and CCP subsidies found by Professor Sumner and others constitute "significant" price-suppression. Given the conditions of competition in the world market for cotton, price effects of 1 or 2 percent would be significant. Contrary to the U.S. arguments, the evidence before the Panel demonstrates that the effect of the U.S. marketing loan and CCP subsidies and the payments made thereunder is (i) significant price suppression in the world

market for cotton, in violation of Articles 5(c) and 6.3(c) of the *SCM Agreement*, and (ii) an increase in the U.S. world market share, in violation of Articles 5(c) and 6.3(d) of the same *Agreement*.

Removal of Step 2 Did Not Impact the Price Suppressing Effects of Marketing Loan and CCP Subsidies

25. In the context of this Article 21.5 proceeding, the repeal of the Step 2 program constitutes a non-attribution factor. In the words of the original panel, the issue is whether the Step 2 program in MY 2005 "would have the effect of attenuating th[e] causal link, or of rendering not 'significant' the effect of" marketing loan and CCP subsidies.

26. The U.S. Government itself confirms that the repeal of Step 2 has minimal effects on the revenue protection enjoyed by U.S. cotton producers. Other independent studies also find relatively modest effects from the repeal of Step 2. The United States argues that the smaller amount of U.S. exports in MY 2006 is evidence of the removal of adverse effects by the repeal of Step 2. This is largely false. According to USDA, the decline in U.S. exports is "almost entirely attributable to reduced sales to China," partially due to decreased demand from China and increased exports from India. Second, as the United States has conceded, there was a large and unnatural surge in U.S. exports at the end of MY 2005 just before the termination of the Step 2 program. Nevertheless, USDA's current projections of MY 2006 exports remain at the second highest level in history, at levels that are comparable to MY 2004 and 22 percent above MY 2002 levels.

Statement of Andrew Macdonald

27. Due to its large size and the availability of reliable information, the U.S. cotton market is the single most important market influencing cotton prices throughout the world. China has undoubtedly an influence on the world market, but it does not lead world market prices. India is another example of an important cotton-producing and -consuming country. Brazil, like most other cotton producing countries, is a relatively small producer of cotton and its domestic market consumes the majority of its production. None of the other cotton-producing countries individually have the export potential needed to assert a substantial influence on price trends.

28. The U.S. elimination of the Step 2 program for cotton on 1 August 2006 was well received by the cotton producers outside of the United States. The effect of Step 2 on the international market is extremely difficult to judge under such a complex system. Yet, Macdonald believes that international cotton prices were initially somewhat higher than they would have been if the Step 2 program had been maintained. However, what might have been gained in terms of increased price levels from its elimination has most likely been lost by the accumulation of larger stocks in the United States. Under normal circumstances, such increased stocks would result in a reduction of production in the United States, which would be the only way for U.S. prices to rise. However, the remaining domestic support programs give U.S. producers little incentive to react to such price signals.

3. EXPORT CREDIT GUARANTEES

29. With respect to three ECG programs maintained by the U.S. Commodity Credit Corporation – GSM 102, GSM 103 and SCGP – the DSB recommended that the United States withdraw the subsidy and otherwise bring itself into compliance with its obligations by the implementation deadline of 1 July 2005. However, U.S. "measures taken to comply" with the DSB's ECG-related recommendations do not exist in some respects. To the extent they do exist, they are not consistent with the export subsidy rules of the *Agreement on Agriculture* and the *SCM Agreement*.

30. Brazil has demonstrated that there is no credit protection product available in the marketplace that is comparable to a GSM 102 ECG. Accordingly, the GSM 102 program offers a unique financial

instrument without any parallel at market, and therefore confers "benefits" *per se*. In Brazil's view, that is the beginning and the end of the analysis.

31. Brazil has also demonstrated quantitatively that GSM 102 fees are lower than fees for comparable products offered by ExIm Bank, by an average of over 100 percent of the GSM 102 value. The United States has never disputed the accuracy of Brazil's ExIm Bank comparison. Instead, it criticizes Brazil for not benchmarking GSM 102 fees against fees for products offered by three multilateral institutions – the EBRD, the IDB and the IFC. The United States criticizes Brazil for arguing that because these three <u>entities</u> are public rather than private, they cannot offer commercial <u>products</u>. The United States goes on to argue that fees charged by these entities are market-based or "commercial" (without providing any indication of what these fees are, or how they compare to GSM 102 fees). This argument is peculiar, for at least two reasons.

32. **First**, it may or may not be true that public <u>entities</u> like the EBRD, IDB and IFC can offer commercial <u>products</u>. Brazil tends to think it is not true. However, the exhaustive evidence offered by Brazil to demonstrate that GSM 102 fees fall far below fees for comparable ExIm Bank products stands. Like the EBRD, IDB and IFC, the ExIm Bank is a public entity. Despite its status as a public <u>entity</u>, the United States presumably considers that the ExIm Bank offers commercial <u>products</u>, including the products used by Brazil in its benchmarking analysis. If so, then Brazil fails to understand why the ExIm Bank benchmarking analysis provided by Brazil is any less probative than would be an analysis involving EBRD, IDB and IFC fees. Brazil has demonstrated that GSM 102 fees fall below ExIm Bank fees for comparable products. If the United States believes that the result would be <u>different</u> in a comparison between GSM 102 fees, on the one hand, and EBRD, IDB or IFC fees, on the other, it is up to the United States to prove it. If the United States does <u>not</u> consider that the ExIm Bank products used by Brazil in its benchmarking analysis are provided on terms consistent with market, <u>then those products themselves confer a "benefit"</u>. In that case, by using ExIm Bank products as a reference point for assessing GSM 102 ECGs, Brazil is being unduly generous to the United States.

33. **Second**, the United States has previously argued that export credits offered by public entities can not be considered commercial products. The Panel can therefore understand Brazil's surprise at the United States' insistence that EBRD, IDB and IFC products provide relevant benchmarks. Brazil tends to agree with the standard the United States apparently applies to WTO Members other than itself – that is, that a public or government entity is not the commercial market. While the United States finds significance in the fact that public entities like the EBRD, IDB and IFC are "profitable" (whatever the definition of that term), making a "profit" does not mean that fees charged by a public entity are consistent with market. A public entity can charge below-market fees and still make a "profit", particularly because its costs are below those faced by its market-based counterparts. A market-based entity must charge fees high enough to make a profit on costs higher than those faced by its public or government counterparts, and the profit must offer a sufficient return to attract capital from investors. "Profitability" of a public entity is not an adequate measure of the full extent of the "benefit" conferred by a government financial contribution.

34. Turning to the role of Article 14(c) of the *SCM Agreement,* the United States criticizes Brazil for not having undertaken a quantitative assessment of "benefit" under the calculation methodology included in Article 14(c). In the United States' view, the <u>only</u> way to determine whether a "benefit" has been conferred by a guarantee subject to export subsidy claims under the *Agreement on Agriculture* and Part II of the *SCM Agreement* is to assess the effect of the guarantee on the price of an underlying loan.

35. Article 14(c) is <u>not</u> the sole standard to determine whether a government guarantee confers a "benefit" in a dispute under the *Agreement on Agriculture* and Part II of the *SCM Agreement*. Article 14 applies solely "[f]or the purpose of Part V" of the *SCM Agreement*, or in other words, for

proceedings involving countervailing measures, where calculation of a duty is required. The "guidelines" in Article 14 support the conclusion that Article 1.1(b) of the *SCM Agreement* embodies a "benefit to recipient" standard. Unlike in countervailing duty proceedings, where a duty must be calculated, disputes under Part II of the *SCM Agreement* do not require quantification of the "benefit" found under Article 1.1(b). Thus, Article 14 does not prescribe hard and fast rules, even in countervailing measure disputes, to which the provision is explicitly applicable. Outside the context of countervailing measure disputes, this flexibility to account for the factual circumstances at hand is at least as important to preserve.

36. Brazil makes an alternative argument under item (j) in the event the Panel does not consider Brazil's evidence and argument to be sufficient to show that GSM 102 fees confer "benefits" and constitute subsidies under Article 1.1 of the *SCM Agreement*. Brazil asks the Panel to determine whether the GSM 102 program constitutes an export subsidy under the so-called "break even" standard in item (j). This evidentiary point stands, without painting Brazil into the imaginary interpretive quandary constructed by the United States.

37. Even if the United States has withdrawn the elements of the GSM 102 program that made it an export subsidy under item (j) (a proposition with which Brazil does not agree), it has "replace[d] the original subsidy with yet another" prohibited subsidy – the provision of export-contingent GSM 102 ECGs at below-market fees. It has, therefore, failed to achieve "full withdrawal" of the subsidy consistent with the Article 4.7 recommendation. In urging the Panel not to examine whether its replacement measure confers export-contingent "benefits", the United States seeks precisely to escape its obligation under that provision to fully withdraw the prohibited subsidy.

38. Contrary to the U.S. position, item (j) does not, *via* an *a contrario* reading, constitute the only evidentiary path by which an export credit guarantee or an ECG program can be shown to constitute an export subsidy. There is one very important reason for this conclusion – item (j) does not satisfy the terms of footnote 5 of the *SCM Agreement*. Footnote 5 expressly identifies the only circumstances in which the Illustrative List can be relied upon to identify measure that are not prohibited. Item (j) does not in any way affirmatively refer to any ECGs as "not constituting export subsidies." It therefore cannot be read *a contrario*, as the United States wishes. This same conclusion was reached by the panel in *Korea – Vessels*, which considered item (j) in light of footnote 5.

39. The first category of evidence relates to the *structure and design* of the GSM 102 program. This evidence is critical, because it is an ECG program's structure and design that ultimately determine whether the fees charged will, over the long term, cover operating costs and losses. Viewed alone, historical data about an ECG program's performance is potentially unreliable, because it may reflect accidents of good fortune over a given period of years.

40. Brazil has identified at least five aspects of the GSM 102 program that establish that it is not structured and designed to meet its long-term operating costs and losses. All of these structural features were considered by the original panel to support its conclusion that the ECG programs constituted export subsidies within the meaning of item (j). All of these structural features persist in the amended GSM 102 program.

41. Brazil turns now to the second category of evidence that is relevant to the compliance Panel's analysis under item (j) of the Illustrative List, should the Panel deem it necessary to proceed to that alternative basis for finding GSM 102 to be an export subsidy. That second category comprises Brazil's evidence that, as a matter of *historical* performance, the GSM 102 program has not met its operating costs and losses. Brazil has offered such evidence using both a net present value methodology, and a cash basis accounting methodology. Viewed using either methodology, the GSM 102 program does not survive scrutiny under item (j).

42. To close, Brazil made a brief observation on its claim that no measures taken to comply exist with respect to ECGs for unscheduled products and rice outstanding on 1 July 2005. Brazil's claim is supported by the compliance panel and Appellate Body reports in *Brazil – Aircraft (21.5)*. These reports concluded that in continuing, after the implementation deadline, to perform on financial instruments concluded before adoption of the DSB's recommendation, Brazil was not fully withdrawing the subsidy. Analogously, in continuing, after the implementation deadline, to perform on ECGs issued before adoption of the DSB's recommendation, the United States has not fully withdrawn the subsidy. We believe that as a result, the United States can neither pay claims under these outstanding ECGs, nor reschedule those outstanding ECGs.

ANNEX C-2

CLOSING STATEMENT OF BRAZIL

(28 February 2007)

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1. Introduction

1. Thank you Mr. Chairman, Members of the Panel and Members of the Secretariat. In our Closing Statement, we would like to touch upon a few issues in the U.S. Oral Statement of yesterday.

2. Relationship of Article 21.5 of the DSU and Article 7.8 of the *SCM Agreement*

2. This Panel is well aware that this is the first Article 21.5 proceeding to deal with implementation of rulings related to adverse effects under the *SCM Agreement*. Brazil cannot over-emphasize the importance of an interpretation that safeguards the effectiveness and legal integrity of the provisions under Part III of the *Agreement*. As the United States reminded us in its Oral Statement, "[a]n interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility."[1]

3. I recall the question that I posed yesterday in our Oral Statement: When the original panel issued its report on 18 June 2004, did the original panel intend to leave Brazil with no implementation rights for serious prejudice caused by mandatory and price-contingent marketing loan and CCP program payments made after 31 July 2003 – the end of MY 2002?

4. If the United States were to prevail on its view that <u>subsequent</u> mandatory and price-contingent marketing loan and CCP <u>payments</u> are not properly before this Panel, the grant of annual recurring subsidies becomes "a moving target that escape from [the WTO subsidy] disciplines."[2] Subsequent mandatory subsidies would always have to be subject to new dispute settlement proceedings, and by the time these proceedings were completed, the effects of the latest subsidies would be superseded by yet more subsidies, which could in turn only be challenged in yet another original panel process. WTO dispute settlement would dissolve into a "Groundhog Day" situation, with no remedy available to Members suffering adverse effects.[3]

3. Price Transmission and Market Integration

5. In its Oral Statement, the United States claims that Brazil makes conflicting arguments by arguing (i) for a rapid price transmission in an integrated world cotton market and (ii) for a much slower predicted reaction by farmers outside the United States to higher prices from the elimination of U.S. cotton subsidies. Andrew Macdonald and Professor Sumner both discussed these issues. The United States confuses two related, but distinct issues.

6. Much of world's cotton is produced in relatively remote areas, often lacking strong infrastructure. Further, information systems for farmers are often limited and in some cases policies restrict the ability of farmers to respond to world market prices. These conditions mean that farmers' planting decisions in some countries respond incompletely, or with some delay, to observed changes in world market prices for cotton.

7. At the same time, the world market for cotton is well integrated. Prices are highly correlated over time across various country markets. The CIF price charts that the United States exhibited with its Oral Statement show that prices for cotton in different countries move together. But those CIF prices are not the prices that farmers observe directly in those countries. In fact, there is a major step

[1] Appellate Body Report, *U.S. – Gasoline*, p. 23.

[2] Panel Report, *U.S. – Softwood Lumber IV (21.5)*, para. 4.30.

[3] Panel Report, *U.S. – Softwood Lumber IV (21.5)*, para. 4.30, quoting arguments of the European Communities.

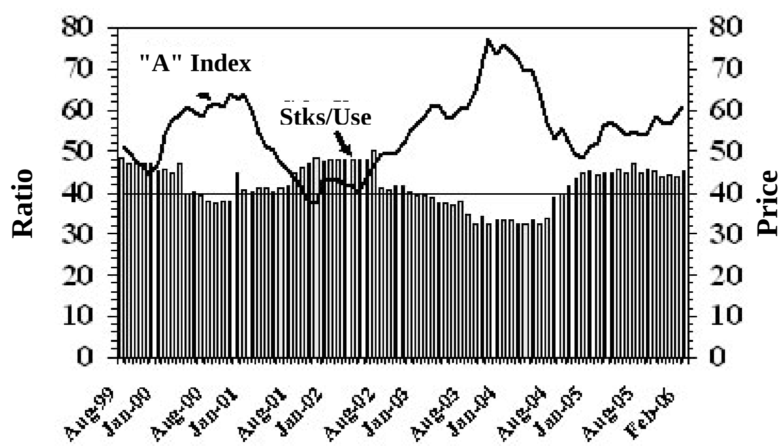
from the CIF export price at the border and retransmissioning those price signals back to individual farmers. Hence, these prices confirm market integration, but do not reflect the slow and limited price transmission that affects cotton farmers' planting decisions.

8. Consequently, the United States, in paragraph 80 of its Oral Statement[4], misinterpreted a statement by Professor Sumner regarding the transmission of prices. The statement at paragraph 28 of Annex I notes that "there is an imperfect transmission of price changes generated by U.S. cotton policy changes to cotton producers in certain cotton producing regions." As I think we can agree, foreign growers will react more slowly to "policy changes" taking place in the United States than would a U.S. cotton farmer faced with the imminent elimination of its own revenue from marketing loan and CCP subsidies. This is obviously different from the daily price fluctuations of the New York futures or "A Index."

4. BRAZIL'S CAUSATION ANALYSIS, EXPORTS AND THE EFFECTS OF STEP 2

9. In its Oral Statement, the United States claims that Brazil has shifted position from asserting that exports cause price suppression, to asserting that stocks and production cause price suppression. The United States misinterprets Brazil's claims. Production, stocks and exports are in fact interlinked; any production not consumed domestically must eventually be exported. Moreover, as the graph in the written version of my statement demonstrates[5], cotton prices and the relative amount of stocks are closely correlated. In other words, subsidy-fueled production that results in stocks impacts market prices, much as subsidy-fueled production that results in exports.

**Cotton: "A" Index and World Stocks/Use,
August 1999 – February 2006**



10. As Andrew Macdonald has explained, for purposes of price effects, U.S. stocks and exports are one and the same. In light of declining U.S. domestic use, U.S. stocks must eventually be exported. The transparency of the U.S. market means that market participants are fully aware of this fact. Whether U.S. supply ends up temporarily in a warehouse, or is exported immediately, the U.S. subsidies-generated supply suppresses world market prices.

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[4] Check against delivery version.

[5] Exhibit Bra-660 (http://www.cottoninc.com/CottonMarketComments/ChinaStocksRevisedUpward/).

11. Further, the United States claims that the repeal of the Step 2 program has reduced U.S. exports, as allegedly shown by MY 2006 year-to-date data. Yet, the data show that after years of increases, exports from almost all the large exporting countries (except India, which is a special case given the improvements in the Indian cotton industry) are projected to fall in the current marketing year.[6]

EXPORTS	**2000-2001**	**2001-2002**	**2002-2003**	**2003-2004**	**2004-2005**	**2005-2006**	**2006-2007**	**05/06 v 06/07 % Change**
WORLD	5881	6449	6645	7233	7780	9645	8769	-9.99
USA	1472	2395	2591	2995	3143	3821	3418	-11.79
CFA	755	756	815	1957	936	1031	971	-6.18
UZBEK	800	810	783	659	850	1000	946	-5.71
AUSTRALIA	849	662	575	470	435	538	483	-11.39
BRAZIL	68	147	107	110	339	456	330	-38.18
GREECE	270	250	280	247	321	355	243	-46.09
INDIA	n/a	n/a	11	119	136	600	894	32.89

in '000 metric tons Source ICAC – World Cotton Statistics – Review of Cotton Situation[7]

12. USDA itself has stated what many independent market analysts, including Andrew Macdonald, confirm: that Chinese demand for imports has fallen considerably as China is apparently using up "a large supply of cotton imported prior to the expiration of the Step 2 program."[8] Increasing Indian exports have added to export declines in the United States and other exporting countries.[9]

13. Nevertheless, USDA (and ICAC) currently project U.S. exports in MY 2006 to be the *second highest in history* and comparable to MY 2004 levels. The United States has conceded that MY 2005 saw a large and unnatural surge in exports just prior to the repeal of Step 2.[10] Thus, the level of exports would probably have been lower in MY 2005 and higher in MY 2006 *but for* the unusual end of MY 2005 surge of exports taking advantage of the last Step 2 subsidies. Indeed, U.S. MY 2007 exports are projected to increase again.

14. In sum, there is no evidence that the elimination of Step 2 has any significant impact on U.S. exports.

5. COST OF PRODUCTION

15. The United States claims that Brazil's "theory" of a cost-revenue gap "fails as a matter of fact"[11] because of newly-presented cost/revenue data for MY 2003. As Brazil noted in its

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[6] Exhibit Bra-652 (International Cotton Advisory Committee Review, Volume 60, Number 3 January-February 2007, accessed February 2007, p. 4).

[7] Exhibit Bra-661 (Export Statistics, ICAC, February 2007).

[8] Exhibit Bra-662 (Elton Robinson, "High certificated cotton stocks slow trade, weigh on prices," Delta Farm Press, 1 December 2006, accessed February 2007 at http://deltafarmpress.com/mag/farming_high_certificated_cotton/).

[9] Exhibit Bra-652 (International Cotton Advisory Committee Review, Volume 60, Number 3 January-February 2007, accessed February 2007, p. 4.

[10] Exhibit Bra-651 (Cotton and Wool Outlook, USDA, 12 February 2007, p. 4, accessed February 2007 at http://usda.mannlib.cornell.edu/usda/current/CWS/CWS-02-12-2007.pdf).

[11] U.S. Oral Statement, para 71 (Check against delivery version).

Oral Statement[12], MY 2003 was characterized by unusually high prices. Over the past seven years (*i.e.*, MY 1999-2005), MY 2003 is the only year, in which the average U.S. acre planted to cotton happened to make a profit based on market revenue. That said, even the United States admits that in MY 2003 fully 8 percent of U.S. cotton production was unable to cover its variable and total costs. Based on this MY 2003 data, the United States implies that over the lifetime of the 2002 Farm Act, "fully 92 percent of U.S. upland cotton is produced without the help of subsidies."[13] However, this is wrong even for MY 2003. The average middle cost farm covered costs, but within the group, there is also a wide range an many of those farms (about a third depending on the precise nature of the variation of those farms) failed to cover costs. This means that, even in MY 2003 almost half of the U.S. production failed to cover costs.

16. Moreover, as we demonstrated yesterday and in previous submissions, this is false. MY 2003 is the odd year in which the U.S. cotton industry earned $864 million. In the four years prior to MY 2003 and the two years thereafter, it lost $13.2 billion. Unless my math is wrong, a profit of $864 million hardly offsets a loss of $13.2 billion, but results in long-term net *losses* of $12.4 billion that were covered by marketing loan and CCP subsidies.[14] There is no basis for the U.S. assertion that U.S. cotton production is economically viable.[15]

6. "SIGNIFICANT"

17. The United States argues that Brazil failed to establish that the world market price effects from marketing loan and CCP subsidies are "significant." We have addressed this issue in our submissions, and again in yesterday's statement. According to the original panel, "significant" means "important; notable … consequential"[16] and must be assessed in light of the market and product at issue.[17] The original panel moreover clarifies that for cotton "a relatively small decrease or suppression of prices could be significant because … profit margins may ordinarily be narrow" and "because of the sheer size of the market in terms of the amount of revenue involved in large volumes traded."[18]

18. We have presented quantitative evidence of price effects based on Professor Sumner's study. His results fall right in the middle of a range of work by other economists. In light of the product and market at issue, the price effects he finds are "significant." For example, in MY 2005, the value of total cotton production was $31 billion.[19] Applying Professor Sumner's average price effect of about 10 percent represents revenue of $3.1 billion – a result that is significant by any measure.

19. By contrast, the United States has presented a remarkable economic conclusion to the Panel that is clearly at odds with mainstream economics. It claims that U.S. marketing loan and CCP subsidies cause price suppression of between 0.96 and 2.26 percent depending on the time period examined and the U.S. parameter set selected. Compare these numbers to the helpful table prepared by FAO listing a variety of estimates from a variety of sources.[20] The U.S. estimates are not just at the low end of the table. They have fallen off the table below the lowest points in the range of even

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[12] Brazil's Oral Statement, para. 84.
[13] U.S. Oral Statement, para. 86 (Check against delivery version)
[14] Exhibit Bra-477 (U.S. Upland Cotton Costs and Returns).
[15] Exhibit Bra-477 (U.S. Upland Cotton Costs and Returns).
[16] Panel Report, *U.S. – Upland Cotton*, para. 7.1325.
[17] Panel Report, *U.S. – Upland Cotton*, para. 7.1329.
[18] Panel Report, *U.S. – Upland Cotton*, para. 7.1330.
[19] Brazil's First Written Submission, para. 190.
[20] Exhibit Bra-579 ("Cotton: Impact of Support Policies on Developing Countries – Why Do the Numbers Vary?" FAO Trade Policy Brief, p. 2, accessed December 2006 at ftp://ftp.fao.org/docrep/fao/007/y5533e/y5533e00.pdf).

the lowest estimates of any other analyst. As Professor Sumner points out in his supplementary statement in Exhibit Bra-659, the set of parameters put forward by the United States as the basis for these estimates is not credible. Their results are incredible actually.

20. In any event, in light of the product and market at issue, even the price effects found by the United States must be considered "significant." In light of the very competitive nature of the cotton market, profit margins of developing country cotton producers, including in Brazil and in West African countries, are generally low. Assuming conservatively that they reach 5 percent, a one percent price effect would increase farmers' net income by 20 percent. Very small price effects, therefore, have a large impact on their income and livelihood, as is evident from Chad's presentation this morning.[21] The United States appears to argue that these effects are "unimportant," "not notable," or "inconsequential." The United States is wrong.

Finally, the original panel also noted that the 5 percent *ad valorem* subsidization rate set out in Article 6.1(a) of the *SCM Agreement* may be relevant in assessing "significance."[22] In this regard, I note that the subsidization rates of U.S. cotton from marketing loan and CCP subsidies alone averages 40 percent over the period MY 2002-2005, and reaches 61 per cent in MY 2004.[23]

7. EXPORT CREDIT GUARANTEES

21. I have a few closing comments on ECGs. The United States has not demonstrated that the amended GSM 102 program meets its long-term costs and losses, under item (j). Applying a net present value (NPV) methodology, as did the original panel, the CCC continues, every year, to project that GSM 102 ECGs issued in that year will result in losses.

22. The NPV calculation used to arrive at initial projections of losses on ECGs actually issued in a given year is critical, whether or not re-estimates are made over time. U.S. law requires NPV projections because they "measure more accurately the costs of Federal credit programs" than does cash-basis accounting.[24] Similarly, bank regulators all over the world use projections of default probabilities and losses-given-default – the core of NPV methodology – to gauge the adequacy of a bank's capital.[25] If historical experience truly establishes that a methodology overstates the risk of default, the methodology may be adjusted accordingly for the purpose of calculating future projections on new commitments. The CCC makes such adjustments; FAS has stated that "credit models used to calculate the subsidy for the guaranteed credits were revised in FY 2001 and FY 2003 and currently provides reliable estimates".[26] Despite these adjustments, the CCC continues to project cohort-specific long-term losses upon issue of each new GSM 102 cohort.[27]

23. But let us assume, for the sake of argument, that the United States has amended the GSM 102 program so that it now meets its costs and losses. This does not mean that the United States has lived up to its obligation to "withdraw the subsidy", for two reasons.

[21] *See* Panel Report, *U.S. – Upland Cotton*, para. 7.54 and additional references thereto.
[22] Panel Report, *U.S. – Upland Cotton*, footnote 1432.
[23] Brazil's First Written Submission, Table 6.
[24] Exhibit Bra-545 (2 U.S.C. § 661(1)).
[25] *See* "Internal Ratings-Based Approach" of the Basel Committee on Banking Supervision", described at http://www.bis.org/publ/bcbs128.htm.
[26] Exhibit Bra-588 (Agricultural Export Credit Guarantee Programs Assessment, ExpectMore.gov, Section 3.CR2) (emphasis added).
[27] *See* evidence cited in Brazil's Opening Statement, para. 253.

24. First, the United States is wrong that item (j) "demonstrates dispositively the circumstances under which export credit guarantees are considered export subsidies".[28] This argument would transform an "illustrative" into an exhaustive, dispositive list. The U.S. interpretation also fails to give full effect to footnote 5. A provision that tells us what is an export subsidy does not automatically tell us what is not an export subsidy. For example, all we know from item (j) is that, if a program fails to meet its costs and losses, it is an export subsidy. It is neither correct interpretively, nor logically valid, to conclude that if an ECG program breaks-even, it is not an export subsidy. Mere implication, through *a contrario* reasoning, does not satisfy footnote 5. Rather, to satisfy that footnote, the item must actually contain language that "refer[s]" to a measure as "not constituting" an export subsidy.

25. Second, the Appellate Body has found that "full *withdrawal* of a prohibited subsidy … cannot be achieved by a 'measure taken to comply' that replaces the original subsidy with yet another subsidy found to be prohibited."[29] Thus, even if the amended GSM 102 program clears item (j), the United States has merely replaced it with another export subsidy. Under the amended fee schedule, GSM 102 ECGs are export-contingent contributions that confer "benefits", in two senses.

26. First, GSM 102 ECGs confer "benefits" *per se,* because they are unique financial instruments with no parallel at market, and because they enable credit that would not otherwise be available.[30] The United States has not provided a single example of a product offered by a market-based entity that imparts the essential qualities of a GSM 102 ECG cited by Professor Sundaram.[31] The United States has offered precisely one example of a bank that was able to secure a commercial loan without a GSM 102 ECG. Even that one example involved an investment grade bank, rather than the non-investment grade foreign obligors targeted by GSM 102.[32] Brazil's evidence and argument stand.

27. Second, Brazil has demonstrated that GSM 102 fees are dramatically lower than fees for essentially identical products offered by a non-market U.S. government entity, ExIm Bank. The sole U.S. response is that other non-market entities – the EBRD, IFC and IDB – also offer products that it alleges are similar to GSM 102 ECGs. The United States does not, however, explain why these non-market benchmarks would offer a better comparison than that offered by Brazil's ExIm Bank exercise. Nor has the United States demonstrated that GSM 102 fees are higher than fees for these allegedly similar products offered by the EBRD, the IFC and the IDB.

28. According to the United States, the only way to determine the existence of a "benefit" from an ECG in an export subsidy case is through a quantitative assessment under what it deems the "total cost of funds" approach in Article 14(c).[33] However, this overlooks the wording and role of Article 14. That provision sets forth only "guidelines" that the Appellate Body, at the United States' urging, has concluded must not be followed rigidly, even in countervailing measure disputes to which the provision expressly applies.[34] That flexibility is even more important to preserve in an export subsidy case, where Article 14 does not directly apply, precisely because the quantification foreseen by the provision is not required. All Brazil need show is that some "benefit" flows from a GSM 102 ECG.

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[28] U.S. Opening Statement (Check against delivery version), heading III.A.1 (emphasis added).

[29] Appellate Body Report, *U.S. – FSC (21.5 II)*, para. 83 (italic emphasis in original; underlining supplied).

[30] *See* Brazil's Opening Statement, paras. 174-177.

[31] Brazil's First Written Submission, Annex III (Statement of Professor Rangarajan Sundaram), para. 7.

[32] Brazil's Opening Statement, paras. 218, 223.

[33] U.S. Opening Statement (Check against delivery version), paras. 31-39; U.S. Rebuttal Submission, paras. 137-144; U.S. First Written Submission, paras. 107, 133-134, 138.

[34] Appellate Body Report, *U.S. – Softwood Lumber IV,* para. 92.

29. Two panels have held that a guarantee confers a "benefit" if it is offered at fees that are not consistent with market.[35] In the particular factual circumstances of this case, where the U.S. exporter does not bear the cost of extending or securing credit, an evaluation of the GSM 102 fees paid by the exporter is particularly appropriate.[36] Insisting on the rigid "total cost of funds" approach supported by the United States would be interpretively wrong, and would also risk the very "circumvention" of the subsidy disciplines that led the Appellate Body to its flexible approach to Article 14.[37]

30. I offer a closing note on our claim that no measures taken to comply exist with respect to certain ECGs outstanding on 1 July 2005. The original panel found that the ECG programs were export subsidies within the meaning of item (j). The recommendation that the United States "withdraw the subsidy" therefore applied to the ECG programs. However, the recommendation also includes the subsidiary obligation to withdraw certain outstanding ECGs issued under those programs.[38] Continuing to perform on such ECGs, defined in Article 1.1 as contingent liabilities, does not satisfy the definition of "withdraw" offered by the Appellate Body in *Brazil – Aircraft (21.5)* (or, for that matter, by the United States in its opening statement). Paying a claim on default of a GSM 102 credit does not "remove" or "take away" the subsidy[39], or "cause" that subsidy "to decrease or disappear".[40]

8. CONCLUSION

31. Thank you Mr. Chairman and Members of the Panel for your time and attention. We look forward to provide responses to answer your written questions.

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[35] Panel Report, *EC – CVDs on DRAMs*, para. 7.189; Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.345.

[36] Brazil's Opening Statement, para. 205; Brazil's Rebuttal Submission, paras. 402-407, 411-413.

[37] Appellate Body Report, *U.S. – Softwood Lumber IV*, para. 100.

[38] Appellate Body Report, *U.S. – FSC (21.5)*, paras. 2, 223-231 (recommendation to withdraw a subsidy in the form of an overarching measure, the FSC, includes the obligation to stop making pre-committed payments to existing FSCs); Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45 ("… to continue to make payments under an export subsidy measure found to be prohibited is not consistent with the obligation to 'withdraw' prohibited export subsidies, in the sense of 'removing' or 'taking away'.").

[39] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45.

[40] U.S. Opening Statement (Check against delivery version), para. 42.

ANNEX C-3

EXECUTIVE SUMMARY OF THE OPENING STATEMENT OF THE UNITED STATES

(27 February 2007)

1. This is a compliance proceeding. The question for this Panel is whether Brazil has established that the U.S. measures taken to comply with the DSB's recommendations and rulings are inconsistent with the covered agreements cited by Brazil.[1] The burden is on Brazil to prove its claims in this regard. The United States has taken numerous steps to comply: (a) the United States stopped operating the Supplier Credit Guarantee Program (or "SCGP"); (b) the United States ceased operating the GSM 103 program; (c) the United States overhauled GSM 102, the remaining export credit guarantee program; and (d) the United States eliminated the Step 2 program. As a result, the United States is in compliance with its WTO obligations.

I. CLAIMS IN RESPECT OF EXPORT CREDIT GUARANTEES FOR EXPORTS OF UNSCHEDULED PRODUCTS AND RICE

2. **– GSM 102 Guarantees Issued Subsequent to 1 July 2005 Are Provided Consistently with Item (j) of the Illustrative List.** Brazil argues that, notwithstanding any U.S. measures taken to comply, GSM 102 guarantees are inconsistent with Articles 10.1 and 8 of the *Agreement on Agriculture* and 3.1(a) and 3.2 of the *SCM Agreement*. These claims turn largely on a single question – whether the GSM 102 guarantees are "export subsidies" under the *SCM Agreement*.

3. There is only one definition of "export subsidy" in the *SCM Agreement* and its elements are set out in Articles 1.1 and 3.1(a) of the *SCM Agreement*. To show how *these* definitional elements apply in particular circumstances, Article 3.1(a) refers to the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*. In the case of export credit guarantees, it is item (j) that applies. Item (j) "illustrates" – or "clarifies" – those export credit guarantees that *are* export subsidies (*i.e.*, those that are provided under programs "at premium rates which are inadequate to cover the long-term operating costs and losses of the programs") from those that are not. This was how the original panel determined whether the GSM 102, GSM 103, and SCGP export credit guarantees were providing "export subsidies" in the original proceeding. This was also the basis for the DSB's recommendations and rulings regarding the guarantees. And this was the analysis that the United States observed in implementing the DSB's recommendations and rulings.

4. The United States has taken a number of measures to increase the premiums and lower the potential long-term operating costs and losses of the portfolio of export credit guarantee programs examined by the original panel. The financial data in the U.S. budget shows now that the export credit guarantee programs operate at entirely profitable levels, consistent with item (j).

5. **– Articles 1.1 and 3.1(a) Do Not Establish a "Different Benchmark" From the One in Item (j) For Establishing Whether Export Credit Guarantees Are Export Subsidies.** Brazil has provided no credible rebuttal to the U.S. evidence regarding item (j). It has concentrated its efforts, instead, on finding a "back-door" way to attack the guarantees. Toward this end, it has claimed an "entitlement" to challenge GSM 102 guarantees under the general definitional elements in Articles 1.1

[1] DSU Article 21.5.

and 3.1(a) and then, if it fails in that regard, to raise an argument under item (j) "in the alternative."[2] Brazil's approach is based on an incorrect interpretation of the *SCM Agreement*. Contrary to Brazil's arguments, "Articles 1.1/3.1(a) and item (j)" do *not* "offer . . . *different benchmarks* to demonstrate that a measure is an export subsidy."[3] Indeed, such an interpretation leads to entirely untenable results.

6. Brazil argues that the U.S. approach would require what Brazil terms an "*a contrario*" reading of item (j). According to Brazil, footnote 5 of the *SCM Agreement* allegedly "definitively forecloses" such an interpretation.[4] This is incorrect, as Brazil itself has recognized in other disputes.[5] Contrary to Brazil's arguments, footnote 5 does not require an "affirmative statement" that a measure is *not* a prohibited export subsidy, and an "affirmative statement" is not required under the ordinary meaning of the term "refer." To the contrary, the ordinary meaning confirms that "referred to" can include measures that are either *expressly* or *implicitly* "referred to" as not constituting export subsidies.[6] Brazil explained to the Appellate Body, in *Brazil – Aircraft (21.5)* that item (j) contains just such an implicit reference.[7] Moreover, the Appellate Body indicated that it accepted Brazil's argument that the first paragraph of item (k) could be read *a contrario* to determine when measures are "justified."[8] That result is equally appropriate here.

7. Brazil's interpretation of footnote 5 is undermined also by the negotiating history, which shows that Members agreed to delete from an earlier draft language that would have required an *express* reference in order for the provisions of the footnote to apply.[9] Moreover, that interpretation would – if applied – nullify or render redundant a number of provisions of the *SCM Agreement*, including footnote 5 itself. As the Appellate Body has explained, "[a]n interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility."[10]

8. **– Brazil Has Not Shown That GSM 102 Guarantees Provide a "Benefit."** The Panel's analysis properly ends with an assessment under item (j). Any further examination, however, would only confirm that the GSM 102 guarantees are not prohibited export subsidies, as Brazil fails to demonstrate any distinct "benefit" under Article 1.1(b). Indeed, Brazil attempts to show a "benefit" based on a theory that, if credited, would undermine not only item (j) and other provisions of the *SCM Agreement* – for the reasons noted above – but also the logic of Articles 1.1(a) and Article 14(c) of the *SCM Agreement*.

9. Article 14 does not apply directly in this context; it applies, instead, "for the purpose of Part V" of the *SCM Agreement*. Nonetheless, because it interprets and applies the definition of "benefit" set out in Article 1.1, it has been relied upon by the Appellate Body as important contextual guidance in interpreting "benefit,"[11] and, indeed, it has been invoked by Brazil to justify its approach here.[12] Article 14(c) provides that a government loan guarantee confers a benefit for countervailing

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[2] Brazil Rebuttal Submission, para.457.

[3] Brazil Rebuttal Submission, para.470 (emphasis in original).

[4] Brazil Rebuttal Submission, para.563.

[5] *See e.g., Brazil – Aircraft (AB)*, paras. 14 and 19.

[6] *See* Oxford English Dictionary, p. 2520 (Exhibit US-116).

[7] *Brazil – Aircraft (AB)*, para. 19.

[8] *Brazil – Aircraft (21.5) (AB)*, para. 80.

[9] *Compare* MTN.GNG/NG10/W/38/Rev. 2 (2 November 1990) and MTN.GNG/NG10/W/38/Rev. 3 (6 November 1990).

[10] *United States – Gasoline (AB)*, p. 23.

[11] *Canada – Aircraft (AB)*, para. 155.

[12] Brazil First Written Submission, paras. 371-375

duty purposes *only* where there is "a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee." The "benefit" is measured as "the difference between these two amounts adjusted for any differences in fees."

10. Article 14(c), thus, recognizes that the provision of a loan guarantee is fundamentally different from the provision of other government services. In the case of government services, Article 14(d) applies and provides that a "benefit" may be calculated only where "the provision [of the service] is made for less than adequate remuneration." Article 14(c) specifically *precludes* such an approach for loan guarantees. Instead, it recognizes that a loan guarantee is made for the sole purpose of *supporting a loan transaction*; the guarantee becomes an integral part of that transaction and has no value beyond it. An assessment of the total costs of the transaction is necessary to assess whether a "benefit" is actually conferred by the guarantee. A simple comparison of the fee charged for the issuance of one loan guarantee to the fee charged for another may provide an incomplete and distorted picture in this regard.

11. Brazil purports to invoke Article 14(c) of the *SCM Agreement* to support its approach.[13] But under the guise of identifying a "severable benefit," Brazil actually attempts to conduct the kind of simple comparison of fees that *Article 14(d)* allows for assessing whether a government-provided service confers a benefit, but that *Article 14(c)* specifically *precludes* with respect to loan guarantees.

12. Brazil has not even attempted to make the kind of particularized showing contemplated under Article 14(c) of the *SCM Agreement*. Instead, Brazil relies on sweeping and erroneous assertions that obligors on loans guaranteed under the GSM-102 program can *never* obtain any other financing of any kind and that the United States could *never* provide an export credit guarantee without also providing an export subsidy. These arguments simply do not square with the evidence submitted by the United States showing that such obligors are, in fact, able to obtain financing even without GSM 102 guarantees and on terms better than those available *with* GSM 102 guarantees. The declining level of use of the GSM 102 program in recent years is even further evidence of this.

13. Moreover, even though they are not part of the inquiry under Article 14(c), Brazil's other sweeping theories – including of GSM 102 guarantees being a unique financial instrument – have been shown to be factually unsupported. These arguments too are unavailing in the face of the evidence of financial products entirely comparable with those offered by the United States from private, profit-seeking entities that are not agencies or instrumentalities of any government. In short, Brazil has not demonstrated that GSM-102 guarantees presently confer export subsidies.

14. **– Measures Taken to Comply Exist With Respect to GSM 102, GSM 103, and SCGP Guarantees Issued Prior to 1 July 2005.** With respect to these measures, the U.S. obligation was to "cause to decrease or disappear" or "take away" the provision of "the service under the export credit guarantee programs" at a "net cost to the government, as the service provider."[14] The United States has done so.

15. There is no merit to Brazil's attempts to call into question the fact that SCGP guarantees have expired on the basis that the United States is continuing to *recover* money on claims that it has paid out on SCGP guarantees in the past. Nor is there any basis for Brazil's argument that the United States is not permitted to make itself whole by collecting on claims paid out on export credit guarantees that were issued prior to 1 July 2005.

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[13] Brazil First Written Submission, paras. 371-375

[14] *Upland Cotton (Panel)*, para. 7.804.

16. Moreover, nothing in the *SCM Agreement* provides that "withdrawing" a "subsidy" allegedly "taking the form of a program" "includes an obligation to abstain from performing on commitments outstanding under that program as of the deadline for implementation."[15] That argument improperly equates "performing on commitments under the program" with the "subsidy" itself. Such an equation was appropriate in *Brazil – Aircraft (21.5)*, where Brazil continued to issue new WTO-inconsistent bonds even after the period of implementation on the basis that it had pre-existing contractual obligations to do so.[16] However, it is not accurate here, where the guarantees are not themselves prohibited subsidies.

IV. ACTIONABLE SUBSIDY RELATED CLAIMS

17. A number of erroneous assumptions must be made even to get to the merits of Brazil's actionable subsidy related claims in this proceeding. The Panel must simply assume, despite the express statements to the contrary in the original panel report, that the original panel's "present" serious prejudice finding extends to the Step 2, marketing loan, and counter-cyclical payment *programs* and *all payments* authorized thereunder. Moreover, despite the fact that the original panel could not have known the *actual* market conditions – and did not examine the *likely* market conditions – in MY 2006, the Panel must also assume that the original panel made a finding that "present" serious prejudice would exist at this time as a result of the measures challenged in the original proceeding. As there is no basis on which to make any of these assumptions, Brazil's claims fail at the outset. There are also more flaws if one probes further.

18. **– Brazil Fails to Substantiate Its Arguments That Termination of the Step 2 Program Was Effectively Meaningless**. The evidence and arguments submitted by Brazil regarding the termination of the Step 2 program are difficult to credit. They are unsubstantiated, internally contradictory and inconsistent with arguments that Brazil made in the original proceeding on such fundamental issues as the effects of Step 2 payments on exports and world market prices.

19. Indeed, Brazil's submissions are almost devoid of any acknowledgment that Brazil argued and, indeed, convinced the original panel to declare the Step 2 program to be a prohibited export subsidy. Export subsidies are prohibited because they are "dependent for [their] existence on export performance" and are specifically "'tied to' the export performance."[17] They are, thus, by definition expected to induce exports and deemed so likely to distort trade that no examination of their actual trade effects is required under the *SCM Agreement* in order for a finding against them.

20. Having convinced the original panel to make an export subsidy finding against the Step 2 program – in response to which the United States eliminated the program completely – how can Brazil now allege that termination of the program has "no impact on the level of U.S. . . . exports"? Moreover, given that Brazil's theory of price suppression centres on whether U.S. upland cotton is exported, how can Brazil now allege that elimination of that allegedly *export-contingent* subsidy has "little positive impact on the world price for cotton in the long term"?[18] These are questions to which Brazil has yet to provide a credible answer.

21. Moreover, while Brazil may now consider termination of the Step 2 program to be inconsequential, the loss of the program has not been meaningless to U.S. producers and exporters. Since the termination of the program, U.S. exports are at exceptionally low levels – the United States

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[15] Brazil Rebuttal Submission, para. 396.

[16] *Brazil – Aircraft (AB)*, para. 45.

[17] *Canada – Aircraft (21.5 – Brazil) (AB)*, para. 47.

[18] Brazil First Written Submission, para. 206 (quoting Brazil First Written Submission, Annex II, paras. 41-43).

discussed some of these statistics at start of this presentation – and the forecasts for this marketing year and the next continue to be poor. It is simply too early to know precisely how much of this decline is attributable to the loss of the Step 2 program. Undoubtedly some of it is not. But what is clear is that Brazil's assertion that termination of the Step 2 program has "no impact on the level of U.S. production or exports" and "little positive impact on the world price for cotton" finds little basis in the empirical evidence. The evidence, in fact, supports exactly the opposite conclusion.

22. **– Brazil Does Not Demonstrate That Marketing Loan and Counter-Cyclical Payments Are Causing "Present" Significant Price Suppression.** Nor are marketing loan and counter-cyclical payments presently significantly "suppressing" world market prices within the meaning of Articles 5(c) and 6.3(c) of the *SCM Agreement*. Brazil's theory, in general terms, is that "payments-cause-overproduction-cause--price-suppression." To support its theory, though, Brazil would have to: (a) submit persuasive evidence showing that marketing loan payments and counter-cyclical payments are *actually* inducing U.S. farmers to plant more cotton than they otherwise would; (b) show that the *degree* of effect on U.S. farmers' planting decisions, production, and export is such as to have impacts on world market prices; and (c) submit evidence to show that the *degree* of effect on world market prices is "significant" within the meaning of Article 6.3(c). Brazil has not done so.

23. **Evidence Regarding *Actual* Production Decisions and Effects of Payments Undermines Brazil's Claims.** In assessing the evidence and arguments submitted by Brazil, it is important to bear in mind that a claim of "present" serious prejudice under Articles 5(c) and 6.3(c) requires a showing that significant price suppression *actually* exists under the prevailing market conditions. Brazil cannot simply allege – or attempt to show – that marketing loan and counter-cyclical payments have the *potential* to induce production. It is also important to note that Articles 5(c) and 6.3(c) are concerned with the *effects* of subsidies, not their form. Thus, Brazil's efforts to show that marketing loan and counter-cyclical payment programs provide income support in times of low prices do not go far. Nothing in the *SCM Agreement* or any other agreement prohibits income support categorically.

24. Given Brazil's particular theory of planting effects leading to price effects, it is necessary to examine the actual planting decisions made by U.S. farmers. At a minimum, any assessment must be grounded in the understanding that in each year when a farmer sits down to decide whether to plant cotton, he does not *know* with certainty (a) what prices will be for cotton at the time of harvest, (b) what prices will be for competing crops at that time, (c) what his yields will ultimately be, (d) whether he might ultimately get a marketing loan payment on cotton or other crops, and (e) whether the season-average farm price for the upcoming marketing year will ultimately be below the threshold at which he might receive a counter-cyclical payment with respect to any upland cotton *base acres* that he holds. The farmer's planting decision *must* be made on the basis of *expectations*.

25. While Brazil has acknowledged (at least some) of these basic facts of upland cotton production[19], little of the evidence and arguments submitted by Brazil actually take these facts into account and show – on the basis thereof – significant production effects under the market conditions prevailing at present. By contrast, the United States has submitted evidence that takes into account the actual operation of the marketing loan and counter-cyclical payment programs and shows *minimal* effects on production, including (a) recent studies, (b) a nationwide survey of farmers' planting considerations, (c) evidence that much of counter-cyclical payments is passed through to non-operator landowners in the form of higher rents and land values, data showing that substantially less upland cotton (40 percent less) is planted by holders of upland cotton base acres today than at the time base acres were set, (d) data showing that a significant and growing portion of U.S. upland cotton planted acreage is on farms with cotton planted acreage that exceeds cotton base acres, or, indeed, on farms with no cotton base acres, and (e) evidence showing that futures prices for harvest-time contracts were

[19] *See e.g.,* Brazil First Written Submission, Annex I, para. 36 (emphasis added).

above the marketing loan rate in MY 2006 and that, even in earlier years when they were not, the evidence shows that U.S. farmers' planting decisions were driven by market factors, not expectation of payments under the marketing loan program. This evidence contradicts Brazil's theory that marketing loan and counter-cyclical payments have significant effects on planting.

26. Brazil purports to demonstrate *indirect* production effects through its claim that U.S. planting, production, and exports are not responsive to prices. However, Brazil's comparisons are flawed in that they ignore basic facts of upland cotton production; for example, by comparing planting decisions in a marketing year to the *actual* prices that develop many months later[20] or to the futures prices of upland cotton *alone*.[21] Moreover, the theory that Brazil advances of alleged market insulation is at variance with the empirical evidence. Indeed, Brazil's theory depends on the notion that the income support provided by marketing loan and counter-cyclical payments causes U.S. farmers to produce and U.S. exporters to export when anticipated low prices cause producers and exporters elsewhere to pull back. If that were true, one would expect to see U.S. share of world production and world exports increase. But that is not what one finds. Rather, U.S. share of world production and exports has been stable over the entire period of the FSRI Act and, indeed – in terms of production – for many years before that as well. This shows that, contrary to Brazil's arguments, U.S. producers and exporters have reacted to market signals in their production and exports in a similar way to their foreign counterparts.

27. Brazil has argued that U.S. producers cannot meet their total costs without marketing loan and counter-cyclical payments. Brazil asserts that this shows that without marketing loan and counter-cyclical payments, many U.S. producers would not have remained in business and continued planting upland cotton. **Table A.1**[22] shows, however, that the overwhelming majority of U.S. production (*92 per cent*) takes place on low- and mid-cost farms that meet both their variable (or operating) costs and also their total costs of production. This means that, for *92 percent of U.S. production* of upland cotton, Brazil's theory of a cost-revenue gap fails as a matter of fact. In other words, with respect to 92 percent of U.S. production, it is not necessary even to reach the arguments regarding the other flaws in Brazil's reasoning regarding the alleged cost-revenue gap. That gap simply does not exist.

28. There *are* other problems in Brazil's analysis as well, including the fact that Brazil incorrectly assumes that total costs of producing upland cotton are determinative for both year-to-year planting decisions and for longer-term decisions, such as whether to continue or exit upland cotton farming. In the former case, it is variable costs that are relevant and, in the latter, it is the *total* cost/revenue balance of the farm – of which costs and revenues for upland cotton is one factor – that is relevant. Moreover, the evidence shows that U.S. producers not only meet their variable costs with market revenue from sales of upland cotton, but also their total costs.

29. **Brazil Has Not Submitted Reliable Evidence Regarding the Degree of Any Price Effect.** The *only* evidence that Brazil has submitted purporting to examine the price effects of marketing loan and counter-cyclical payments specifically are the results of the modeling exercise that it has conducted for purposes of this proceeding. That exercise is conducted using a model that is entirely different from the one advanced by Brazil in the original proceeding, but that is virtually identical to one that was published in 2005, in a CATO institute publication, by Dr. Sumner, Brazil's economist. In the CATO publication, Dr. Sumner warned that his model "abstract[s] from many complexities that would be important to get more precise estimates" and that "[t]he simple model laid out here does not

[20] *See e.g.*, Brazil First Written Submission, paras. 144-145.

[21] *See e.g.*, Brazil First Written Submission, paras. 142-143 and Brazil Rebuttal Submission. paras. 221-224.

[22] Exhibit US-119.

represent the depth of analysis that would be appropriate to support a trade remedy proceeding or a serious prejudice claim before a WTO panel."[23] The United States agrees.

30. We have identified a number of the key problems with Brazil's new model. These include that the model: (a) lacks cross-commodity impacts and cross-price elasticities, potentially leading to biased price effects; (b) is static with no explicit relationships for changes in cotton stock levels and no stocks equation; (c) contains foreign supply elasticities that are different from FAPRI that underestimate the response of foreign producers to changes in world prices; (d) treats production flexibility payments and direct payments differently even though they operate in the same way; (e) incorporates Step 2 payments directly into the producer revenue function as fully coupled payments, and (f) appears to ignore statutory parameters, for example by including counter-cyclical payment rates in each of the various price expectations that sometimes exceed the statutory maximum. These are just some of the problems that stem from the structure of the model itself, and the simplified, reduced nature of the assessment it attempts to conduct.

31. Even more significant biases result from the flawed econometric parameters used by the Sumner II model. Although Brazil has indicated that its new model "employs many of the same parameters used in the model and analysis submitted to the original panel, as well as parameters commonly used by USDA and Food and Agricultural Policy Research Institute ("FAPRI") economists,"[24] this is untrue. As shown in Table A-2 (Exhibit US-120), the elasticity estimates used by the Sumner I model (which were purported to be "FAPRI-based") and the Sumner II model differ in each case except for the estimate of the U.S. mill demand elasticity.

32. These differences matter because they can – and do – have dramatic effects on the estimated outcomes. As shown in Table A.2, not only does the Sumner II model use different elasticities than the Sumner I model, but, in each case, the Sumner II model elasticity results in a greater effect on world price due to an elimination of marketing loans and counter-cyclical payments. Moreover, the Sumner II model simply ignores the demand for US and world cotton stocks. Yet, as Brazil has acknowledged, year-to-year fluctuations in stock levels are important factors in any credible analysis of world cotton markets.[25] The modifications made by Brazil exaggerate the effects of the elimination of marketing loans and counter-cyclical payments on world cotton price.

33. Brazil has not provided any valid basis for discarding the generally-accepted economic parameters that it recognized, itself, as being appropriate in the original proceeding. As Brazil argued at that time, the FAPRI econometric model is well-established, well-known and widely used.[26] It is also valuable inasmuch as its calculations and parameters have not been developed in conjunction with any specific dispute or on behalf of any specific party. The FAPRI model has a strong foundation within economic circles and is well-respected. The Sumner II model, by contrast, has no foundation within economic circles. Although Dr. Sumner argues that the departures from FAPRI-based parameters indicate "improvements based on . . . continued research," Brazil has not identified that "research" and has provided no citation to any independent literature or other established or accepted bases for the new parameters.

34. Brazil has also attempted to justify a number of its flawed econometric parameters on the basis that it is looking to assess the impact of eliminating the marketing loan and counter-cyclical

[23] Daniel A. Sumner. "Boxed In: Conflicts Between U.S. Farm Policies and WTO Obligations." Center for Trade Policy Studies, The Cato Institute, December 2005. (Exhibit US-108)

[24] Brazil First Written Submission, para. 168.

[25] Brazil Oral Statement, 27 February 2007, para. 160.

[26] Brazil Further Submission to the Panel, 9 September 2003, para 214.

payment programs in the short-run, while leaving all else equal.[27] However, under Article 6.3(c) the question is what, if any, degree of price suppression exists *presently* as a result of the marketing loan and counter-cyclical payment programs and whether this degree of price suppression is "significant." To the extent a counterfactual assessment is undertaken, it is only to assess what the price equilibrium would be at present if marketing loan and counter-cyclical payments had been lower, different, or did not exist. Article 6.3(c) does not ask what prices will look like in the short-run adjustment period if the marketing loan and counter-cyclical payments are suddenly eliminated. Indeed, Members are not even required to eliminate measures found to be actionable subsidies; they are given a choice between "withdrawing" the subsidy or removing its adverse effects. Thus, in addition to the fact that the economic literature supports a long-term assessment, Brazil's argument that it is necessary to look at the short-run effects of total elimination of the programs cannot be accurate as a textual matter.

35. Second, it is not credible for Brazil to argue for a disproportionately small rest-of-world supply response on the basis that "there is imperfect transmission of price changes" because "market institutions, centralized crop marketing, government policies, limited information, and high per-unit transportation costs partially insulate producers in certain regions of the world" from any alleged price changes.[28] The United States recalls that Brazil insisted in the original proceeding that different domestic prices were intimately connected and that a change in U.S. prices would be reflected fairly immediately in the prices of all major cotton producers. Moreover, even Brazil has recognized that, in the mid to long run, there is price transmission. It is that response that is properly captured here.

36. **To capture the long run effects of removal of marketing loans and counter-cyclical payments, the United States has also applied parameter estimates taken from the UNCTAD-FAO Agricultural Trade Policy Simulation Model.** The summary results are presented in table A.4 (Exhibit US-122) for the periods MY 2002-2005 and MY 2006-2008. These conservative results – in the range of 0.96 to 2.26 percent – which obtain from some very basic changes to the parameters of Brazil's new model illustrate that the estimates provided by Brazil of price effects in the range of 9-11 percent substantially overstate any possible impact on world market price.

37. **– Brazil Has Not Shown That the Degree of Effect on World Market Prices Is "Significant" Within the Meaning of Article 6.3(c).** In Brazil's first submission, Brazil simply referred back to the same evidence it had submitted purporting to show price suppression and argued that "even a fraction of the effects found by Professor Sumner would constitute price suppression, based on its effect on [the] large volume of sales in the world market."[29] In its rebuttal submission, Brazil did not address the issue at all.

38. There is no textual basis for Brazil's lone theory of "significant" price suppression – that, effectively, any amount of price suppression is "significant" because the world upland cotton market is a high volume market. Brazil's approach would effectively create a *per se* rule of "significant" price suppression for certain markets involving large volumes of sales. Such a rule is not found in Articles 5(c) or 6.3(c) of the *SCM Agreement* or any other provision.

39. Contrary to Brazil's assertions, it is necessary to make a *showing* on the facts of a dispute that any proven price suppression is "significant." Brazil has not attempted to make such a showing here. And, in any event, a finding of "significant" price suppression is not justified under the circumstances. Brazil has provided no basis for its claims that this degree of price suppression – even less than a cent per pound, in conservative terms – constitutes "significant" price suppression. If such unfounded assertions were to prevail, they would effectively write "significant" out of Article 6.3(c) entirely.

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[27] *See e.g.*, Brazil First Written Submission, Annex I, 25-26.

[28] Brazil First Written Submission, Annex I, para. 28.

[29] Brazil First Written Submission, para. 190.

ANNEX C-4

CLOSING STATEMENT OF THE UNITED STATES

(28 February 2007)

1. Mr. Chairman, we will end in this meeting where we started, recalling that this is a compliance proceeding pursuant to Article 21.5 of the DSU. The question in this proceeding is whether Brazil has shown that U.S. measures taken to comply with the DSB's recommendations and rulings are inconsistent with the covered agreements cited by Brazil.

2. The United States has taken measures to comply with the recommendations and rulings of the DSB. Let us recall what they are:

- The longer term GSM-103 program is gone.
- The Supplier Credit Guarantee Program is gone.
- The old fee schedule that did not take into account relative risk is gone, replaced by a fee schedule graduated by both risk and tenor, comprised of 6 risk grades of ever-increasing fees. As a result, fees under the schedule have increased 46 percent.
- Obligors in countries that present a worse risk than permitted under the fee schedule are excluded entirely from the GSM-102 program. This is not a static determination simply to exclude certain countries on 1 July 2005. Rather, any country that falls to an unacceptable risk grade will be excluded from eligibility.

3. As a result of the reforms, total guarantees have declined over *63 percent* from $3.7 billion in FY 2004 to $1.36 billion in FY 2006.

4. Mr. Chairman, the United States is fully in compliance with item (j) of the SCM Agreement. Indeed, the data show that the United States was in compliance even before making all of these changes. Certainly, the imposition of these further disciplines only further confirms that.

5. Brazil urges this Panel to ignore the analytical basis for the Panel's original decision, and the clear textual guidance indicating that item (j) "illustrates" dispositively how the general definition of "export subsidy" in Articles 1.1 and 3.1(a) apply. The United States does not agree, but, nonetheless, has shown that – even under Article 14(c) of the SCM Agreement, which Brazil has invoked as context in assessing "benefit" under Article 1.1 – Brazil, which bears the burden of proof in this case, has failed to identify any distinct benefit under Article 1.1.

6. The United States has supplied other real-world examples of commercial banks providing financing comparable to that under the GSM-102 program, but Brazil derides these examples as irrelevant because, despite the explicit language of Article 14(c) of the SCM Agreement, Brazil considers the proper comparison is not of the total costs of the guaranteed loan transaction, but whether only one component of all the elements of the transaction – fees – are on terms more favorable than those provided by a private commercial bank.

7. There is no basis for that interpretation. Brazil is urging the Panel to ignore *both* of the two provisions of the SCM Agreement that specifically talk about the conditions under which export

credit guarantees may be considered subsidies – prohibited export subsidies in the case of item (j) and subsidies subject to CVD actions in the case of Article 14(c). Brazil would have the Panel overlook the fact that *neither* calls for a comparison to fees alone.

8. Mr. Chairman, the market for export credit guarantees is not – and has never been – one in which purely private banks – like Citibank, for example – operate. Indeed, against this background, one can understand why the drafters would – in both item (j) and Article 14(c) use a benchmark *other* than one looking to fees charged for purely private market-provided guarantees.

9. By insisting that the Panel simply ignore the provisions expressly agreed upon by the drafters in item (j) – and, indeed, in Article 14(c) – Brazil is effectively urging the Panel to find that *all* export credit guarantees are *per se* prohibited. Such an interpretation is simply untenable.

10. Returning to the issue of the U.S. measures taken to comply, the United States recalls that it also has eliminated the Step 2 program. This program was found to be a prohibited export subsidy, as well as a prohibited import substitution subsidy, and payments thereunder in MY 1999-2002 were found to cause adverse effects in the same period.

11. These measures – the measures in respect of the export credit guarantee programs and the Step 2 program – are the measures that the United States has taken to comply. Brazil has sought in this proceeding to diminish and dismiss each and every one of these measures while simultaneously attempting to broaden the scope of this proceeding so that the United States will be considered to have failed to have met its implementation obligations. For example, Brazil argues that the marketing loan and counter-cyclical payment programs are "measures taken to comply."

12. Mr. Chairman, this is just a fiction. The Appellate Body has recognized before that measures taken to comply are ordinarily changes made subsequent to the issuance of DSB recommendations and rulings. The marketing loan and counter-cyclical payment programs were in existence at the time of the original proceeding, were even challenged by Brazil in the original proceeding, and they remain the same now. These are not measures that the United States has taken to comply with any recommendations and rulings.

13. The question then is whether they were subject to the original panel's findings of "present" serious prejudice. The United States has submitted detailed arguments as to why they were not. In doing so, the United States has taken into account the fact that Brazil made no "present" serious prejudice claims against the marketing loan and counter-cyclical payment *programs*, that the only claims made by Brazil in respect of those measures were "threat" of serious prejudice claims, and that the original panel expressly stated that it was declining to make even that finding.

14. Nonetheless, the United States has shown that even if one considers Brazil's arguments on the merits, it is without basis. The argument, in essence, is that elimination of the Step 2 program does not eliminate any adverse effects of the "package" of Step 2, market loan, and counter-cyclical payment programs. But, as we discussed yesterday, Brazil's arguments in that regard fail to address the actual market facts that have prevailed since termination of the Step 2 program and are not consistent with Brazil's own arguments in the original proceeding.

15. Like its shifting arguments regarding the impact of the Step 2 program, Brazil's counterpart argument – that the marketing loan and counter-cyclical payment programs continue to have adverse effects – continues to shift. Yesterday we heard – I believe for the first time in this proceeding – that it is *unsold stocks* and not exported surplus that is responsible for the alleged price suppression. The fact is, Mr. Chairman, it is too late in the day for Brazil to be altering such fundamental factors as its theory of price suppression. And, in any event, Brazil has submitted no evidence or argument to substantiate this new assertion.

16. Brazil's claims regarding the marketing loan and counter-cyclical payment programs fail for a single fundamental reason. They are not supported by the evidence. Much of Brazil's oral presentation again stressed its premise that large payments necessarily show large effects. As Brazil admitted before the Appellate Body, however, this is not correct. While the size of payments is undoubtedly a consideration – and likely an important one – the focus of an adverse *effects* claim is, not surprisingly, on *effects*.

17. We pointed out before that empirical evidence does not support Brazil's arguments regarding price effects (*i.e.*, that payments-cause-production-cause-exports-cause-price suppression). Presumably, in response to this, Brazil, in its presentation yesterday, supplied a slew of charts purporting to show that year-to-year decisions to plant upland cotton are economically irrational. As we discussed earlier, Brazil's analysis fails because it relies on an inappropriate measure of costs that is not relevant to U.S. farmers' planting decisions year-to-year.

18. Beyond this, the only real "evidence" that Brazil presents appears to highlight are the results of the *new* Sumner model, one that abandons most of the economic constructs that Brazil previously argued were accurate and superior. Brazil has offered an economic model without foundation or publication in any peer reviewed journal. Then, Brazil altered virtually every critical economic parameter used by that model to inflate its result. The United States has shown why the model is flawed and why its economic parameters are unreliable.

19. Using reasonable and realistic parameters, even Brazil's model shows small effects from the U.S. programs.

20. Indeed, this confirms what other evidence – recent studies of the empirical data, actual assessments of year-to-year planting decisions (taking into account proper variable costs), and evidence of the stable share of U.S. production and export market share – already shows; namely, that payments under the marketing loan and counter-cyclical payment programs are not having the kind of significant price effects that Brazil has alleged.

ANNEX C-5

THIRD PARTY ORAL STATEMENT OF ARGENTINA

28 February 2007

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Mr Chairman, members of the Panel:

I. INTRODUCTION

1. Argentina is grateful for this opportunity to give its views on the issues raised in the present Panel proceedings. In this oral statement, we wish to address some of the parties' arguments that we did not discuss in our written submission and which concern the United States' submission of preliminary issues to the Panel.

2. Argentina would like in particular to refer to the United States' objection to the inclusion of the marketing loan and counter-cyclical payments programmes in these Article 21.5 proceedings.

II. ARGUMENTS

THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS PROGRAMMES ARE WITHIN THE SCOPE OF THE PRESENT DSU ARTICLE 21.5 PROCEEDINGS

3. The United States asserts in its submissions[1] that many of Brazil's claims are beyond the scope of Article 21.5 proceedings. In particular, in response to Brazil's claims against the programmes authorizing marketing loan and counter-cyclical payments, it states:

(a) That they are not original measures that were subject to Panel findings and recommendations, and

(b) that they are not measures the United States took to comply with DSB recommendations.

4. For the reasons set out below, Argentina strongly disagrees with both assertions and with the United States' arguments supporting them:

A. THE PROGRAMMES AUTHORIZING MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS ARE ORIGINAL MEASURES THAT WERE SUBJECT TO FINDINGS AND RECOMMENDATIONS

5. First, in Argentina's view it is obvious that the original Panel considered these programmes as *measures at issue* in its final Report (section G) when discussing Brazil's actionable subsidies-related claims and allegations of serious prejudice.

6. In particular, in paragraph 7.1107 of its Report, in identifying the measures at issue the Panel includes under (ii) marketing loan programme payments; under (iv) counter-cyclical payments; and specifically, under (ix), the last indent, "**legislative and regulatory provisions currently providing for the payment of measures in (i), (ii), (v), (vi) and (vii) above**."[2]

7. Accordingly, in Argentina's view, to the question whether the programmes ordering marketing loan payments and counter-cyclical payments were part of the "matter at issue" in the original proceedings, the only valid reply is an affirmative one.

8. Secondly, Argentina observes that, contrary to what the United States contends, not only were the programmes among the measures at issue, they were also subject to the Panel conclusions and

[1] First Written Submission of the United States, Section IV(B) and (C); United States' Rebuttal Submission, Section II(B).

[2] Emphasis added.

recommendations, subsequently confirmed by the DSB, as can be seen from Chapter VIII of the Report, which sets out the Panel's conclusions and recommendations. Specifically, the Panel concludes, in paragraph 8.1(g):

> "[…]
>
> (g) concerning serious prejudice to the interests of Brazil:
>
> (i) the effect of the **mandatory price-contingent United States subsidy measures**[3] – marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments – is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*; […]"

9. Then, at paragraph 8.3(d), regarding the subsidies that are the subject of the above-mentioned conclusion the Panel states, citing Article 7.8 of the *SCM Agreement*:

> "[…], upon adoption of this report, the United States is under an obligation to 'take appropriate steps to remove the adverse effects or … withdraw the subsidy'".

10. Consequently, as emerges from the text of the Panel's report, the mandatory price-contingent United States subsidy measures, i.e. *the legislative and regulatory provisions* for payments under the marketing loan and counter-cyclical payments programmes are subject to Panel recommendations.

11. Thirdly, and as confirmation of the foregoing, what the Panel said in paragraphs 7.1499 and 7.1501 – cited by Brazil in its submission of 16 January last – is most enlightening: it states unequivocally that:

> "[…] our finding of "present" serious prejudice thus pertains also to measures in force and subsidies paid in MY2002, the first year of the FSRI Act of 2002."
>
> And goes on to say:
>
> "Because the Panel's "present" serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002, the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice finding. We recall that, pursuant to Article 7.8 of the *SCM Agreement*, the United States is under an obligation to "take appropriate steps to remove the adverse effects or … withdraw the subsidy"."

12. In the light of the foregoing, Argentina sees no merit in the United States' assertion that the <u>programmes</u> authorizing marketing loan and counter-cyclical payments were not subject to findings and recommendations by the original Panel.

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[3] Emphasis added.

B. THE PROGRAMMES AUTHORIZING MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS ARE PART OF THE NEW BASKET OF MEASURES TAKEN TO COMPLY

13. As to the second point, the United States contends that Brazil's claims against the marketing loan and counter-cyclical payments programmes are beyond the scope of the present proceedings because they are not United States "*measures taken to comply*"; and that they are unrelated to the existence or consistency with a covered agreement of measures taken to comply with recommendations and rulings of the DSB, as the programmes remain unchanged.[4]

14. Argentina agrees with Brazil that what we have here is a new basket of mandatory price-contingent measures as a result of the cancellation of the Step 2 programme, one of the measures the United States took to comply with the DSB's recommendations.

15. In Argentina's view it is also worth pointing out that there is no claim seeking to challenge some unchanged aspect of the measure which was not already challenged in the original proceedings, or which was challenged but found to be consistent – rather the contrary. Nor is there a claim that seeks to impugn separate measures which have undergone no change since the original proceedings. As Brazil says, what we have here is a new measure or "new basket of measures", to use the Panel's expression.

16. Furthermore, given the particularities of subsidy regulation, the *SCM Agreement* does not require an analysis of the adverse effects of actionable subsidies to be carried out for each and every programme or payment. Rather, it focuses on the "collective effect" of the subsidies, the approach the Panel followed. Otherwise, there is every likelihood that individually, they would not be sizeable enough to cause adverse effects. Consequently, the finding of serious prejudice affects "a basket of measures" and cannot be split so as to relate to each one separately.

17. Argentina takes issue with the United States' assertion that the fact that the Panel considered the effects of the programmes and payments cumulatively in determining the existence of present serious prejudice does nothing to change the fact that they are separable.[5] Argentina believes that although they may be separated for the purpose of a descriptive study of their structure, design and operation, they are not separable from the legal standpoint of establishing the makeup of the serious prejudice, in accordance with the terms of the Panel's collective finding.

18. Consequently, bearing in mind the Panel's conclusion that "**the effect** of the mandatory price-contingent United States subsidy measures […] is **significant**[6] price suppression […] within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*", it is necessary to reconstruct the collective analysis in order to ascertain whether the change brought about to this set of measures by the cancellation of the Step 2 programme is sufficient to conclude that the United States has complied with the DSB's recommendations in this regard.

19. The Panel's conclusion in paragraph 7.1503 of the report is enlightening here:

> "We consider that, upon required implementation by the United States of this Panel's prohibited subsidy findings and present serious prejudice findings, the basket of measures in question may be so significantly transformed or manifestly different from the measures that are currently in question that it is not necessary or appropriate to

[4] Rebuttal Submission of the United States, paragraph 18.
[5] Rebuttal Submission of the United States, paragraph 61.
[6] Emphasis added.

address Brazil's claims of threat of serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*."

20. It may properly be concluded from the above that the Panel's recommendations were directed to a "basket of measures" and not to measures taken individually.

21. Argentina therefore takes the view that the programmes authorizing marketing loan and counter-cyclical payments are part of the new basket of measures taken to comply, and as such fall within the scope of the Article 21.5 proceedings.

III. CONCLUSION

In the light of all the foregoing, Argentina respectfully asks the Panel to take into consideration the arguments and views expressed above when reaching its decision on the preliminary issues raised by the United States.

Thank you very much.

ANNEX C-6

THIRD PARTY ORAL STATEMENT OF AUSTRALIA

28 February 2007

Members of the Panel,

1. Thank you for the opportunity to present the views of Australia.

2. This proceeding raises a number of important issues concerning the scope of Article 21.5 proceedings and the appropriate steps that must be taken by a Member to comply with Articles 4.7 and 7.8 of the *Agreement on Subsidies and Countervailing Measures (SCM Agreement)*.

3. Australia has provided a written submission addressing some of these issues and will not repeat those arguments today. Rather, Australia will concentrate on whether the United States, by repealing the Step 2 programme, but maintaining the two other price-contingent subsidies (that is, the marketing loan programme payments and counter-cyclical payments), has taken appropriate steps to remove the adverse effects or to withdraw the subsidies under Article 7.8 of the *SCM Agreement* in accordance with the recommendations and rulings of the Dispute Settlement Body (DSB). In considering this question, it is important to bear in mind the nature of Article 21.5 proceedings.

Nature of Article 21.5 proceedings

4. The role of an Article 21.5 panel is to determine the existence or consistency with a covered agreement of measures taken to comply with DSB recommendations and rulings. Its mandate does not extend to relitigation of issues that have been conclusively determined in the original dispute. Such is the case in the present proceedings, where measures continue in existence that have been previously ruled upon and remain unchanged. It is uncontested that two of the challenged price-contingent subsidies, which are by far the largest of the subsidies that were challenged in the original proceedings relative to the subsidy that has been withdrawn, have continued under programmes that have not been changed since the recommendations and rulings in the original dispute were adopted by the DSB. In this situation, the Panel's task is limited to a factual determination to that effect.

5. Should it make this determination, the Panel will then need to consider, on the basis of the supporting economic evidence, whether the maintained subsidies continue to cause adverse effects within the meaning of Article 5 of the *SCM Agreement*.

6. This question cannot be answered by confining the Panel's examination to the effect of the subsidies made in 1999-2002. Such an approach, which appears to be advocated by the United States[1], would undermine the remedy that is provided by Article 7.8 of the *SCM Agreement* – that is, to compel the subsidizing Member to take appropriate steps to remove the adverse effects or withdraw the subsidy. This approach would require a successful complainant to bring a fresh actionable subsidies claim with respect to each set of

[1] *See*, for example, First Submission and Request for Preliminary Rulings of the United States, paras. 45, 146-148; Rebuttal Submission of the United States of America, paras. 17; 33-34.

subsidies made subsequently to those originally found to cause adverse effects. This cannot be the remedy that was contemplated by Article 7.8. Moreover, such an approach would also be contrary to Article 21.1 of the DSU, which recognises that prompt compliance with the recommendations and rulings of the DSB is essential to ensure effective resolution of disputes. Article 21.5 of the DSU promotes this aim.[2]

Turning to Brazil's actionable subsidies claim

7. The question that is central to Brazil's actionable subsidies claim is whether discontinuation of one price-contingent subsidy but continuation of two other price-contingent subsidies meets the requirements of Article 7.8 of the *SCM Agreement*. In examining this question, Australia submits that the analytical approach adopted in the original proceedings is an appropriate one to be followed by this Panel. The original Panel, after making explicit findings as to the trade-distorting effects of each of the challenged price-contingent subsidies individually, [3] found that the effects of these subsidies, considered collectively, caused significant price suppression in the same world market.[4]

8. Taking the original Panel's findings as to the trade-distorting effects of these subsidies into account, this Panel may then consider whether the collective effect of the continuing subsidies (that is marketing loan programme payments and counter-cyclical payments) is significant price suppression in the same world market.

9. Australia notes that if this approach is followed, then the findings in the original proceedings as to the effect of other causal factors that the United States asserts affect the causal link between the United States' subsidies and the significant price suppression cannot be overlooked.[5] Many of those factors are the <u>same</u> factors that were relied upon by the United States in the original proceedings. Australia submits that it is open to this Panel to reach the same conclusions in relation to those factors as were drawn in the original proceedings. Those conclusions were that these factors did not sever the causal link between United States' subsidies for upland cotton and significant price suppression in the same world market. That is, these factors did not "reduce the effect of the mandatory price-contingent subsidies to a level which cannot be considered 'significant.'"[6]

10. Furthermore, Australia agrees with Brazil that in order to determine whether the effect of the two continuing price-contingent subsidies is "present" serious prejudice, it is necessary to examine a recent period for which essentially complete data exists. That period is, according to Brazil, data for marketing year 2005, there being no complete data as yet for marketing year 2006.[7] In fact that year has not yet finished. In agreeing with Brazil's submission, Australia notes that this approach is the one that was adopted by the Panel in the original proceedings.[8]

11. In finding that the effect of the mandatory price-contingent United States' subsidy measures was significant price suppression in the same world market within the meaning of

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[2] *United States – Softwood Lumber IV (Article 21.5 – Canada),* Report of the Appellate Body, WT/DS257/AB/RW, para. 72.

[3] *See*, for example, WT/DS267/R, paras. 7.1295, 7.1302, 7.1303, 7.1308.

[4] *Ibid*., para. 7.1349.

[5] *Ibid*., paras. 7.1344-46; 7.1357-63; *See* also WT/DS267/AB/R, para. 437.

[6] WT/DS267/R, para. 7.1363; WT/DS267/AB/R, paras. 455-457.

[7] Rebuttal Submission of Brazil to the Panel, paras. 23-24.

[8] WT/DS267/R, paras. 7.1198-9.

Article 6.3(c) of the *SCM Agreement*[9], the Panel at first instance had the benefit of extensive economic analysis and modelling presented by Brazil.[10] Updated economic analysis and modelling has been submitted by Brazil in the present proceedings. In Australia's view, this updated economic analysis and modelling represents the same appropriate and conservative economic methodology as that which was taken into account by the Panel in the original proceedings.[11] This data supports Brazil's central assertion that but-for the domestic subsidies at issue, the world price for cotton would be significantly higher.

12. If, as a result of examining the effects of the continued price-contingent subsidies under the marketing loan and counter-cyclical payments programmes, considered collectively and on the basis of the economic evidence presented, the Panel finds that these subsidies collectively cause significant price suppression, then Australia submits that the only conclusion open to this Panel is that the United States has not complied fully with the requirements of Article 7.8 of the *SCM Agreement*. That is, the United States has failed to remove the adverse effects or withdraw the subsidies that were the subject of the DSB's recommendations and rulings, within the meaning of Article 7.8.

Threat of serious prejudice

13. In relation to Brazil's claim in the alternative that the continued subsidies threaten to cause serious prejudice in marketing years 2006 and beyond, Australia submits that it is beside the point for the United States to argue that the programmes under consideration are due to expire in late 2007. The programmes have not expired. There is no guarantee that they will not be rolled over or maintained in another form with adverse effect. Australia therefore submits that the Panel is entitled to consider whether the continuance of subsidies under programmes whose design, structure and operation remain unchanged, would give rise to a threat of serious prejudice.

14. Australia notes that in the original proceedings, the Panel exercised judicial economy with respect to Brazil's claim of threat of serious prejudice relating to the marketing years 2003-2007. The Panel's approach was based on the assumption, since proved to be erroneous, that the statutory and regulatory framework under which the subsidies were granted would be fundamentally altered in response to the Panel's present serious prejudice finding.[12] It is justifiable that Brazil, by seeking a ruling in the alternative concerning the threat of serious prejudice, should wish to avoid this situation being maintained in the future.

15. In conclusion, Australia submits that it is appropriate for this Panel to adopt the analytical approach that was adopted by the Panel in the original proceedings. Given the fact that two of the price-contingent subsidies have continued in unaltered form, it is also appropriate that the original findings, recommendations and rulings relating to those subsidies should form the starting point for this Panel's analysis. The updated evidence submitted by Brazil supports the conclusion that those subsidies, considered collectively, continue to cause adverse effects to the interests of Brazil. Given the continuing adverse effects of these subsidies, Australia submits that the Panel can only conclude that the United States has failed to take appropriate steps to remove those effects or withdraw the subsidy within the meaning of Article 7.8 of the *SCM Agreement,* and has therefore failed to comply fully with the DSB's recommendations and rulings in this dispute.

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[9] *Ibid*., para. 8.1(g)(i).
[10] *Ibid*., paras. 7.1202-9.
[11] *Ibid*., para. 7.1209.
[12] *Ibid*., para. 7.1501.

ANNEX C-7

THIRD PARTY ORAL STATEMENT OF CANADA

28 February 2007

I. INTRODUCTION

1. Good morning Mr. Chairman, members of the Panel, thank you for giving me this opportunity to present Canada's views on particular legal issues raised in this proceeding.

2. Canada's submission addresses three issues. First, Canada submits that the standard for finding a threat of serious prejudice pursuant to Article 5 of the *SCM Agreement* and GATT Article XVI:1 is flexible. In some instances, such as in the case at hand, a threat of serious prejudice may arise when the threat is reasonably foreseeable and ever-present, even if it is not necessarily "imminent". Second, Canada submits that for the purposes of quantifying a benefit under Article 14(c), a commercial comparison is required. Third, Canada submits that the United States' GSM 102 program cannot benefit from an *a contrario* reading of Annex I to the *SCM Agreement*. Item (j) does not allow for an *a contrario* interpretation. The only programs that are excluded by Annex I from the definition of export subsidies in Article 3.1(a) are those explicitly "referred to" in Annex I as not constituting export subsidies.

II. THREAT OF SERIOUS PREJUDICE

3. Allow me, first, to briefly turn to the standard for a finding of threat of serious prejudice. I do not propose to dwell on this issue, but rather refer the Panel to Canada's written submission. However, I will reiterate that the definition of "threat of material injury" in Part V of the *SCM Agreement* should not be imported into the definition of "threat of serious prejudice", in Part III of that *Agreement*. Nothing in Part III of the *SCM Agreement* suggests a strict temporal limitation to the notion of threat of serious prejudice. The standard for threat of serious prejudice is sufficiently flexible to address programs that give rise to an ever-present and reasonably foreseeable probability of massive subsidies to United States' farmers – subsidies that permanently threaten to cause serious prejudice – as well as programs that will imminently cause adverse effects.

4. The U.S. subsidy programs mandate the payment of subsidies upon certain conditions. One of these conditions is the price of cotton falling to a specified level, a condition that has occurred in the past. Given the vagaries of the market, it is probable that the price of cotton will fall again. When that happens, it will again trigger massive subsidy payments. When these payments are made, they *will* again cause WTO Members serious prejudice. The counter-cyclical payment program and the marketing loan program are, therefore, permanently threatening to cause serious prejudice.

III. ARTICLE 14(C)

5. I now turn to Canada's second issue, which involves Article 14(c) of the *SCM Agreement*. Brazil argues that the "GSM 102" program constitutes an export subsidy prohibited by Article 3 of the *SCM Agreement*. In part, Brazil argues that this export credit guarantee, or "ECG", confers a *per se* benefit because it secures financing that would not otherwise be available to the recipient, and that this is contrary to Article 14(c) of the *SCM Agreement.*

6. Canada respectfully disagrees with Brazil. The mere existence of the GSM 102 program is not a *per se* benefit under Article 14(c). Article 14(c) provides that a loan guarantee by a government

does not constitute a benefit unless there is a difference between the amount the recipient would pay on a comparable commercial loan obtained on the market and the amount it pays to the government. The benefit, in such cases, is the difference between those two amounts adjusted for any difference in fees. Brazil may well be correct that GSM 102 confers a benefit within the meaning of Article 1.1(b) of the *SCM Agreement*. However, in accordance with Article 14(c), demonstrating the existence of this benefit expressly requires a comparison with the market.

7. Brazil argues that the GSM 102 program is designed so that the guarantees are provided only in circumstances in which credit would not otherwise be available, that is, where there is no comparable commercial loan. Canada submits that in respect of most financial instruments, it is possible to find a comparable commercial pricing mechanism. In the event that a commercial comparison or evidence of a commercial comparison cannot be found, one can construct a market proxy. Either way, under Article 14(c), one must make a commercial comparison, whether constructed or otherwise.

IV. ILLUSTRATIVE LIST OF EXPORT SUBSIDIES

8. Third, and lastly, Canada submits that item (j) of the Illustrative List contained in Annex I to the *SCM Agreement* does not allow for an *a contrario* interpretation.

9. The United States argues that GSM 102 is not inconsistent with Article 3 of the *SCM Agreement* because the program charges premium rates that are more than adequate to cover the long-term operating costs and losses of the program. As such, the United States argues that GSM 102 is not inconsistent with item (j), and because none of the other items in the Illustrative List are applicable to it, GSM 102 is not an export subsidy prohibited by Article 3.

10. Article 3.1(a) provides that subsidies contingent on export performance, including those illustrated in Annex I, are prohibited. Canada has consistently argued, and at least two panels have agreed, that footnote 5 in the *SCM Agreement* excludes the possibility of implied exceptions to the prohibition on export subsidies. The panels in *Brazil – Aircraft (Article 21.5 – Canada)* and in *Korea – Vessels*, found that, and I quote, "[i]n its ordinary meaning, footnote 5 relates to situations where a measure is referred to as *not* constituting an export subsidy."[1] To this end, those panels considered whether the item at issue of the *Illustrative List* contained one of two things: any affirmative statement that a measure is not an export subsidy or a statement that a measure not satisfying the conditions of that paragraph is not prohibited. The panel in *Korea –Vessels* found that item (j) did not contain such statements, but rather describes certain circumstances in which particular programs do constitute export subsidies. That panel found that item (j) fell outside the scope of footnote 5.

11. The panel in *Brazil – Aircraft (Article 21.5 – Canada)* came to a similar conclusion from the text of Article 3.1(a) itself. The panel found that Annex I contains examples of prohibited export subsidies, and does not purport to be an exhaustive list. The panel found it "highly likely" that there are prohibited export subsidies within the meaning of Article 3.1(a) that do not fall within the scope of Annex I.[2]

12. Thus, even if, as the United States asserts, the fees charged under GSM 102 were sufficient to meet its long-term operating costs and losses, it would mean only that the program is not captured by

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[1] *Brazil – Export Financing Programme for Aircraft: Recourse by Canada to Article 21.5 of the DSU*, Report of the Panel, WT/DS46/RW, adopted 4 August 2000 ["*Brazil – Aircraft (Article 21.5 – Canada)*"], para. 6.36. *See* also *Korea – Measures Affecting Trade in Commercial Vessels*, Report of the Panel, WT/DS273, adopted 7 March 2005, para. 7.195.

[2] *Brazil – Aircraft (Article 21.5 – Canada)*, para. 6.30.

item (j) of the Illustrative List. It would not mean that GSM 102 is not a prohibited export subsidy. Quite apart from item (j), GSM 102 could still be a prohibited export subsidy pursuant to Article 3 of the *SCM Agreement*.

13. This concludes Canada's statement. I would like to again thank the panel for the opportunity to present Canada's views.

ANNEX C-8

THIRD PARTY ORAL STATEMENT OF CHAD

28 February 2007

I. INTRODUCTION

1. Mr. Chairman and Members of the Panel,

2. Chad appreciates the opportunity to present its views to you in this dispute. In its written submission of 5 January 2007, Chad set out its understanding of some of the major legal issues that arise in this dispute. I will therefore not repeat all that is contained in that submission. Rather, I will take this opportunity to highlight some additional issues relevant to the resolution of this important dispute.

II. THE IMPORTANCE OF THE DSU TO LDCS

3. According to Article 3.2 of the DSU, security and predictability are the cornerstones of the multilateral trading system. Article 3.2 further stresses the importance of prompt settlement of situations in which benefits are being impaired and the maintenance of the proper balance between the rights and obligations of Members.

4. These principles of the multilateral trading system, Mr. Chairman, together with the prohibition against unilateral actions to resolve disputes, found in Article 23 of the DSU, provide the foundation for the WTO's rules-based dispute settlement system. This is intended to be a rules-based system in which might does not trump right, in which the law is applied regardless of the economic strength of the parties to a dispute, and in which the smallest actors in international trade can ask for respect of the rule of law and its principles and prevail.

5. Chad's belief in this system motivated it to become a third party when Brazil requested a panel in the original dispute, and it is this same belief that motivates Chad's participation in these proceedings. By this action, Chad has become one of only a handful of least-developed countries that have participated in a WTO dispute settlement proceeding since the establishment of the WTO in 1995.

6. Chad participated particularly *because* it is a least-developed country, and because there are not alternative means for its interests and concerns to be taken into account.

7. Mr. chairman, it is the weakest Members of the WTO that are most dependent on the rule of law in multilateral trade relations. Lacking political or market power, least-developed countries have no other recourse that to ask for respect of the rule of law. As one WTO Member stated in urging a speedy and successful conclusion to the Uruguay Round:

> The least-developed countries, being the weakest and most vulnerable members of the international community, need the rule of law most and are the strongest advocates of multilateralism. ...[1]

8. Without the WTO's dispute settlement system to ensure that rules are obeyed and obligations upheld, therefore, the weak would be at the mercy of the powerful who would be left free to pursue their own individual interest. As former WTO Director-General Moore cogently underlined, the multilateral system "opens up the privileged positions of the powerful to transparency and competition".[2]

9. Rules-based multilateralism demands that WTO Members found to be in violation of their obligations take steps to address those violations. As Brazil has demonstrated, the United States has either taken no steps to implement the rulings and recommendations of the DSB in the original dispute, or where it has taken such steps, it has not fully addressed the adverse effects that continue to affect the farmers of Brazil, Chad, and other African countries.

10. This Panel must therefore send a clear message to the WTO Membership regarding the effectiveness of the dispute settlement system by requiring that the United States, to the extent that it has failed to implement the recommendations and rulings of the DSB, abide by the principles of the rules-based system; principles which, I would add, the United States has repeatedly claimed to endorse.

III. THE IMPORTANCE OF COTTON TO CHAD

11. Chad participated in the original dispute in this case, and continues to participate in these proceedings, because of the critical importance of the cotton sector to Chad's economy and the ongoing damage to that sector caused by US subsidies.

12. Chad is one of the poorest countries in the world. The United Nations Development Programme's Human Development Report of 2005 ranks Chad as the 173rd out of 177 countries based on human development indicators that include like expectancy at birth, the infant mortality rate, and the maternal mortality ratio.

13. It is precisely because of this poverty that Chad is so seriously affected by the US subsidies. The cotton sector in Chad affects approximately 3 million people, out of a total population of about 8.1 million. Cotton exports are the country's third largest export, representing 60 per cent of all non-oil export earnings. Cotton is, therefore, one of Chad's main sources of income, sustains the livelihood of a large portion of its population, and contributes not only to economic development but also to social development. Thus, cotton is a central element in the government's drive towards modernisation, diversification, and the financing of social activities and other needs of Chad's rural citizens.

14. In the Report "*Finding the Moral Fibre: Why reform is urgently needed for a fair cotton trade*", Oxfam concludes the US cotton subsidies have an impact "not simply on balance of payments or debt service."[3] Oxfam states that US cotton subsidies "cause poverty, and Western African farmers

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[1] Statement by Dr. M Isaac Talukdar of Bangladesh to the Forty-Seventh Session of the GATT CONTRACTING PARTIES, SR.47/ST/4, 20 December 1991.

[2] Michael Moore, "Promoting openness, fairness and predictability in international trade for the benefit of humanity", speech delivered to the Inter-Parliamentary Union on 8 June 2001, available at http://www.wto.org/english/news_e/spmm_e/spmm64_e.htm.

[3] Oxfam Briefing Paper Number 69, 18 October 2004, page 2.

are particularly vulnerable." It is for this reason that Chad welcomed the findings of the Panel in this case. The rulings and recommendations of the Panel – if they had been implemented – would have improved the lot of the many poor who depend on cotton production and export.

15. The development and multilateral agencies that have examined this issue have all come to the same conclusion. Respected economic experts from UNDP, the International Cotton Advisory Committee, the World Bank and Oxfam have established the source of the problems facing African cotton farmers are the trade-distorting agricultural subsidies that continue to depress world cotton prices. They have also concluded that the price prospects for cotton and consequently the export shares of low-cost producers, including many African countries, could be improved considerably if developed countries substantially reduced or eliminated support.

16. It is therefore imperative that the cotton farmers of Chad reap the benefits of a prompt implementation of the DSB's rulings and recommendations in this dispute. Proper compliance would not only stabilise and increase the incomes of Chad's cotton farmers but also develop the economy of Chad as a whole.

IV. THE IMPORTANCE OF COTTON TO THE WEST AFRICAN REGION

17. Chad is not the only West African country that has suffered the effects of the US subsidies. The proper implementation of the DSB's recommendations and rulings is of importance to cotton-producing West African countries, which are some of the most vulnerable economies in the world.

18. The Oxfam report to which I referred above concludes: "every season poor cotton farmers face reduced incomes. Each year, developing countries which export cotton suffer declining balance of payments. The central issue is US cotton subsidies."[4]

19. West and Central African cotton producers are among the lowest-cost producers of the crop in the world. Full implementation by the United States of the DSB's recommendations and rulings in this case would have very significant benefits for Chad and the other Sub-Saharan African cotton-producing countries. A recent World Bank project study titled "WTO's Doha Cotton Initiative: A Tale of Two Issues"[5] specifically estimates what is at stake in terms of cotton production, trade, and economic welfare in Sub-Saharan Africa. The study finds that the removal of *all* cotton subsidies and import tariffs would boost global economic welfare by $283 million per year and would raise the price of cotton in international markets by almost 13 per cent.

20. Chad, together with Benin, Burkina Faso and Mali, is a co-sponsor of the sectoral initiative for cotton which encourages WTO Members to address cotton "ambitiously, expeditiously and specifically" with a view to achieving more ambitious reductions of trade-distorting domestic subsidies for cotton production. This initiative covers not only the subsidies of the United States but also those of other Members of the WTO and it was made explicitly without prejudice to actions of the Dispute Settlement Body. Nevertheless, it can be taken by this Panel as a further indication of the importance that Chad and the other sponsors of the initiative attach to the resolution of the cotton subsidy issue.

21. The commitment made by Members in the context of negotiations should not, however, detract from the importance of this dispute settlement process. The negotiating track is one aspect of the WTO system, the dispute settlement system another. No Member should be put in the position of

[4] *Ibid*.

[5] Kym Anderson and Ernesto Valenzuela, "WTO's Doha Cotton Initiative: A Tale of Two Issues", Development Research Group, World Bank, Washington DC, February 2006.

negotiating afresh an outcome that has already been prescribed multilaterally by the Members acting through the Dispute Settlement Body. Chad asks that it benefit from the enforcement of the negotiated rules governing subsidies and, equally, that it be allowed to gain more from an international market without subsidies and therefore subject to true competition.

22. Chad therefore requests the Panel to ensure, through a careful review of the evidence and rigorous application of the law, that the relevant WTO rules and disciplines are fully applied to the cotton sector so that a fair and market-oriented system can prevail.

23. To quote H.E. Blaise Compaoré, President of Burkina Faso, "our countries are not asking for charity, neither are we requesting preferential treatment or additional aid. We solely demand that, in conformity with WTO basic principles, the free market rule be applied. Our producers are ready to face competition on the world cotton market – under the condition that it is not distorted by subsidies."[6]

V. ARTICLE 24 OF THE DSU

24. Article 24 of the DSU stipulates that: "[a]t all stages of the determination of the causes of a dispute, and of dispute settlement procedures involving a least-developed country Member, particular consideration shall be given to the special situation of least-developed country Members". Chad's reliance on its cotton industry to generate exports and fight poverty constitutes a special situation of a least-developed country Member within the meaning of Article 24. Chad requests the Panel to give full effect to this provision in its determination of the causes of this dispute and to indicate in its report how it has done so.

25. In Chad's view, Brazil has produced compelling arguments and evidence to show that the US price-contingent subsidy programs supporting upland cotton under the FSRI Act have not been withdrawn or changed in any significant way. Brazil has also shown that overproduction and excess exports, along with significantly suppressed world market prices for upland cotton, have continued following the adoption of the reports of the original panel and the Appellate Body in this dispute. As explained above, Chad's own experience confirms the evidence submitted by Brazil.

26. This case concerns egregious, WTO-inconsistent measures taken by a developed country WTO Member that continue to cause serious harm to an important subsistence farming sector in the economies of some of the very least-developed countries in the world. The United Nations Development Programme's Human Development Report concluded that in 2005, "the 20,000 cotton farmers in the United States will receive government payments in 2005 equivalent to the market value of the crop and more than US aid in Sub-Saharan Africa."[7]

27. Chad considers that Article 24 of the DSU imposes a duty on the panel that goes beyond a procedural requirement to consider all the views presented to it (which the Panel is in any event required to do under Article 11 of the DSU), by requiring panels to take into account the special situation of least-developed countries when examining substantive issues. Chad believes that, if the Panel were to ignore and be silent on Article 24 of the DSU in this extreme situation, it would fail to carry out the obligations that this provision clearly assigns to it.

[6] Address to the Trade Negotiations Committee, 10 June 2003, www.wto.org.
[7] UNDP, Human Development Report for 2005, page 132.

VI. CONCLUSION

28. Mr. Chairman, Members of the Panel, it is of critical importance to Chad and other African cotton-producing countries and, indeed, to the multilateral trading system as a whole, that this compliance Panel uphold the rule of law by ensuring that the multilateral rules governing the provision of subsidies are properly applied and followed in this case.

29. In this regard, Chad recalls the statement of the Sutherland Report that:

> The position of the poorest Members of the WTO, the least developed countries, ... has been and should be an issue of increasing concern. If they do not receive real benefit from membership there can be little point in their remaining part of the organization and the moral case for the WTO as a source of good is diminished.[8]

30. In the present case, Chad recalls that Article 7.8 of the SCM Agreement provides that "the Member granting or maintaining such subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy." Article 7.8 therefore requires that the United States take active steps and impose affirmative measures to eliminate adverse effects or withdraw subsidies. The United States cannot comply with the recommendations and rulings of the DSB simply by letting time pass and the adverse effects dissipate.

31. Chad also recalls that the panel stated clearly that "*the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice finding.*"[9] Accordingly, to conform with the recommendations and rulings of the DSB, the United States must not only stop the challenged payments, but also change its legislative and regulatory system.

32. Accordingly, the Panel should carefully and stringently review the measures taken by the United States and determine that the United States has not properly implemented the recommendations and rulings of the DSB.

33. Chad trusts that these views will assist the Panel in its consideration of these issues. Chad will be happy to respond to any questions the Panel may have.

34. Again, we thank you for this opportunity to present our views.

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[8] *The Future of the WTO – Addressing Institutional Challenges in the New Millennium*, Report by the Consultative Board to the Director-General Supachai Panitchpakdi, 2004, paragraph 40.

[9] Panel Report, paragraph 7.1501 (original footnote omitted) (emphasis added).

ANNEX C-9

THIRD PARTY ORAL STATEMENT OF THE PEOPLE'S REPUBLIC OF CHINA

28 February 2007

1. Thank you, Mr. Chairman and Members of the Panel. On 5 January 2007, China provided its third party submission to you on this case. Today, I would like to highlight the major points on two issues in China's submission: (1) whether the item (j) of the Illustrative List of the SCM Agreement constitutes the complete basis for the analysis of GSM-102; (2) whether the ML/CCP payment programs are outside the scope of this proceeding.

2. Firstly, regarding item (j) issue, China believes that the panel's finding in *Korea – Measures Affecting Trade in Commercial Vessels* has provided a useful guidance. The *Korea – Commercial Vessels* panel points out that Item (j) merely describes certain circumstances in which particular programs constitute export subsidies; and Item (j) simply does not address export guarantee programs that do cover their long-term operating costs and losses. Therefore, item (j) does not provide a basis on which to find that measures do not constitute prohibited export subsidies.

3. In other words, item (j) is only a shortcut to determine that an export credit guarantee constitutes an export subsidy when the guarantee does not cover its long-term operating costs and losses. However, it is not a defense clause. Namely, when fees collected for a credit guarantee do cover long-term operating costs and losses for the guarantee, it is still possible that this credit guarantee constitutes an export subsidy, and the panel still needs to examine whether the measure at issue is consistent with Article 1 and 3 of the SCM Agreement or not. In China's view, the definition of export subsides in the meaning of Article 1 and 3 of the SCM Agreement covers a scope much broader than that of item (j) of the Illustrative List. The complainant may raise a *prima facie* case of export subsidy either by claiming an item (j) violation or an Article 1 and 3 violation of the SCM Agreement. Nevertheless, non-existence of the Illustrative List violation does not mean that it also consistent with obligations under Article 1 and 3 of the SCM Agreement.

4. Thus, China considers that the US's approach with regard to item (j) is incomplete, and inconsistent with the provisions in the SCM Agreement.

5. Secondly, regarding ML/CCP payment issue, China cannot endorse the US's arguments. On the one hand, contrary to what the US asserted in its Written Submission, the DSB did make rulings and recommendations in respect to ML/CCP programs in many occasions. For examples, the Original Panel found that: (1) legislative and regulatory provisions of ML/CCP were measures subject to rulings and findings; (2) a textual analysis of the statutes supported that such subsidy programs were 'specific', and (3) ML/CCP payments, among others, were *directly linked to* world prices for upland cotton, and *the structure, design and operation of these measures* constituted evidence supporting a causal link with significant price suppression. In short, the Original Panel did make finding on the ML/CCP programs.

6. In addition, the Original Panel also found that in light of its findings with regard to present serious prejudice, it did not believe that it was necessary to address *Brazil's "threat" claim and "per se" claims relating to these measures*. It is clear that the Original Panel assumed the statutory and regulatory framework of the US mandatory price-contingent subsidy programs should be changed and the Panel therefore refrained itself from making further elaboration in these regards.

7. As to the US's claim that Brazil may not make claims against unchanged measures, China notes that the Original Panel found that the effect of the mandatory price-contingent subsidies was significant price suppression in the same world market and gave rise to serious prejudice to the interests of Brazil. The recommendations and rulings of the DSB accordingly obliged the United States to remove the adverse effects caused by these subsidies, or to withdraw these subsidies.

8. Furthermore, the terms of reference of a compliance panel is not limited to what the responding party claims to be the measures taken to comply. In China's view, since this Compliance Panel is requested to examine whether the measures taken by the United States are consistent with the covered agreement, it is legitimate for the Compliance Panel to examine whether or not the remaining two subsidies (ML/CCP programs) are still causing serious prejudice.

9. This concludes China's oral statement and I thank you very much for your attention, Mr. Chairman and distinguished Members of the Panel.

ANNEX C-10

THIRD PARTY ORAL STATEMENT OF THE EUROPEAN COMMUNITIES

28 February 2007

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Mr. Chairman, distinguished Members of the Panel.

I. INTRODUCTION

1. The European Communities makes this oral statement because of its systemic interest in the correct interpretation of the *SCM Agreement*, the GATT 1994 and the DSU. The European Communities addresses the following issues:

- Panel composition;
- The US requests for preliminary rulings concerning:
  - Export credit guarantees for pig meat and poultry meat under the GSM 102 programme;
  - The marketing loan programme and the counter-cyclical payment programme;
  - Compliance in past periods;
- Certain aspects of the export contingent subsidies claims; and
- Certain aspects of the actionable subsidies claims.

II. PANEL COMPOSITION

2. The European Communities again most respectfully urges the Panel in the strongest terms to exercise its inherent jurisdiction under the *HFCS* case law, and rule on the propriety of its own composition, following the *Australia Automotive Leather II* precedent.[1] This is all the more imperative in the present circumstances because of the obvious and acutely important systemic interest; and the entirely understandable reticence of either Party to expressly intervene at length.

3. The DSU expressly sets out what the "functions of panels" are; and that expressly includes "to assist the DSB in discharging its responsibilities under th[e DSU] and the covered agreements".[2] Those DSB responsibilities clearly include ensuring that panels are properly composed. Article 2(1) of the DSU states expressly that the DSB is established "to administer the[] rules and procedures" set out in the DSU, and that necessarily includes Article 8(3) of the DSU, which relates to panel composition.

4. Furthermore, Article 11 of the DSU requires this Panel to "*assist* the DSB in making the recommendations or in giving the rulings provided for in the covered agreements". The DSB *cannot possibly* have addressed the question of composition at the time of panel request and establishment, since the former post-dates the latter. Therefore, *the only way* in which this Panel can fulfil its obligation to *assist* the DSB in relation to this matter is to deal with it in its report.

III. US REQUEST FOR PRELIMINARY RULINGS

A. EXPORT CREDIT GUARANTEES FOR PIG MEAT AND POULTRY MEAT UNDER THE GSM 102 PROGRAMME

5. The United States request for a preliminary ruling raises a problem being discussed in DSU proceedings with increasing frequency[3]: what is the relationship between the measure at issue (and elements of it) in an original panel; and the measure taken to comply (and elements of it) in a

[1] EC Third Party Written Submission, paras. 6 to 30.

[2] DSU, Article 11.

[3] *See*, for a recent example, Panel Report, *Chile – Agricultural Products (Price Band) (Article 21.5 - Argentina)*, paras. 7.121 to 7.162.

compliance panel. The context of this legal problem includes: 1) the fact that measures at issue may be complex and have many different elements, some of which are more closely interrelated or interdependent than others; 2) the fact that measures at issue may be attacked "as such" (or constitute "programmes" under the *SCM Agreement*) or "as applied" 3) that panel's may focus on resolving the dispute, and thus exercise judicial economy, either with respect to certain claims, or with respect to certain elements of a measure, and that successful appeal of the exercise of judicial economy may be difficult[4]; 4) the principle of *res judicata*, according to which once a matter is decided it should not be re-litigated; 5) the fact that a compliance panel may be followed by immediate retaliation; and 6) that the Appellate Body has no legal basis to "remand" matters to the original panel for re-consideration.

6. The European Communities agrees with the United States that the case law to-date does not yet regulate all aspects of this problem. Specifically, the existing case law does not resolve the question of how the scope of a compliance panel should be determined in circumstances where the exercise of "false" judicial economy is successfully appealed and/or the Appellate Body is unable to complete the analysis.[5] However, the European Communities does not consider that it is by reference to such matters that the problem before you is to be resolved. Rather, it appears to the European Communities that the important issue is the *nexus* or the degree of interrelatedness or interdependence between different elements of the measure.

7. It appears to the European Communities that there are essentially two competing models: "the measure model" (supported by Brazil in this case), which tends to fix the parameters of the compliance panel by reference to the original measure at issue – understanding the measure taken to comply accordingly; and the "element of the measure model" (supported by the United States in this case), which tends to fix the parameters of the compliance panel by reference to the *elements* of the original measure at issue in respect of which findings were made by the original panel, and understand the "measure taken to comply" accordingly. One can find examples of both types of approach in the case law.[6]

8. It appears to the European Communities that neither model may provide a satisfactory method for dealing with all cases.

9. For example, the measure model would appear unsatisfactory in cases involving "as such" claims against Member's legislation implementing the *WTO Agreements* by way of municipal law measures intended to have general and prospective application. These might typically consist of hundreds of articles (or elements). Given the seriousness of "as such" claims, to accept that an entirely new article (or element) could be raised in a compliance panel would appear to be unsatisfactory. In fact, in such cases, typically, it is a particular provision or provisions, and not the piece of legislation as a whole, that is described as the "measure at issue".

10. On the other hand, taken to its logical conclusion, it is not clear where the element of the measure model would stop in its deconstruction or atomisation of a measure at issue. In theory, one could deconstruct a measure at issue into one set of legal elements, one set of factual elements, one set of evidence, and (in some cases) into one set of findings concerning the legal characterisation of facts; and there is no limit in theory to the number of "elements" within each set. It seems to the European

[4] *See*, for a recent example, Appellate Body Report, *US-Zeroing*, paras. 225 and 250 (applying the standard reasoning that additional findings are unnecessary to resolve the dispute).

[5] US First Written Submission, paras. 24 to 30; Brazil's Comments On US Request for Preliminary Rulings, paras. 2 to 15; US Rebuttal, paras. 10 to 15.

[6] *See*, for example, Panel Report, *Japan – Apples (Article 21.5 United States)*, paras. 8.28 to 8.30, where, in effect, the United States argued successfully for the "measure model".

Communities that such an approach might encourage litigants to similarly atomise their claims and arguments, provoking more exercise of judicial economy, appeals from which may not be welcomed by the Appellate Body. It might also encourage litigants to request in parallel and in the alternative and in relation to the same matter a compliance panel *and* a new original panel (eventually with the same panellists) in order to ensure that, whichever model prevails, they do not suffer unnecessary procedural delay – something that would only add needless complexity to already complex legal proceedings.

11. The question therefore poses itself, with particular reference to the facts of this case: are there any objective criteria that can be articulated for determining what approach should be applied? In order to answer that question, in the opinion of the European Communities, the Panel should examine the original measure at issue and the "measure taken to comply", and, with particular reference to the "elements of the measure" that the United States argues are outside the Panel's terms of reference, enquire into the extent to which these are inter*related* or inter*dependent* with measures or "elements of measures" that the United States accepts are within the Panel's terms of reference.[7]

12. It appears to the European Communities that, at first sight, the question of whether or not US export credit guarantees under the GSM 102 programme to pig meat and poultry meat circumvent US commitments for those scheduled products, and are inconsistent with Articles 3.1(a) and 3(2) of the *SCM Agreement*, is not ***necessarily*** inter*dependent* with and arguably not even ***necessarily*** inter*related* with the same question regarding, particularly, upland cotton.

13. However, it also appears to the European Communities that there are other factors that merit careful consideration. For example:

- One particular feature of the *SCM Agreement* is that several of its provisions refer to subsidy "programmes", lending support to the view that a subsidy programme can be a "measure at issue", and further lending support to the view that, ***by its own terms***, such a programme may exhibit a degree of interrelatedness or interdependence between its terms and/or its instances of application.[8]

- The United States appears to have admitted that the GSM 102 programme was and is a "programme" within the meaning of the *SCM Agreement*.[9]

- The original panel consistently described the GSM 102 programme as a "measure at issue", and the United States does not appear to have argued that it in fact consisted of a number of different measures at issue.[10]

- In the original panel Brazil attacked the GSM 102 programme both "as such" and "as applied", although the original panel did not consider this distinction to be a determinative one.[11] There is authority for the view that a compliance panel should consider together both a measure and its *application*.[12]

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[7] Appellate Body Report, *US-Softwood Lumber IV (Article 21.5 – Canada)* (DS257), para. 79 "… the Panel employed a nexus-based test … which accords with our own interpretation of Article 21.5".

[8] *See* final bullet point.

[9] Panel Report, *US-Upland Cotton*, para. 7.811.

[10] Panel Report, *US-Upland Cotton*, para. 7.242.

[11] Panel Report, *US-Upland Cotton*, para. 7.763.

[12] Panel Report, *US-Shrimp (Article 21.5 – Malaysia)*, para. 87.

- In the compliance Panel Brazil has again attacked *per se* the programme, that is, the revised fee schedules for export credit guarantees issued under the GSM 102 programme.[13]

- Finally, and *significantly*, as far as the European Communities can ascertain, the US has ***elected*** to revise the fee schedules for export credit guarantees issued under the GSM 102 ***generally***[14], that is, also for pig meat and poultry meat.[15] In this respect the present case is similar to past cases in which the fact that measures have been ***changed***, suggesting the requisite degree of interrelatedness or interdependence, has tended to bring them within the scope of a compliance panel.[16]

14. The European Communities interest in this matter being systemic, we do not venture a final view on whether or not the GSM 102 programme as it relates to pig meat and poultry meat is or is not within the Panel's terms of reference; but we do respectfully invite the Panel to take the foregoing observations into consideration when reaching its findings on this point.

B. THE MARKETING LOAN PROGRAMME AND THE COUNTER-CYCLICAL PAYMENT PROGRAMME

15. The European Communities agrees with the United States[17] that there is a meaningful distinction between an "as such" claim and an "as applied" claim, although, like most distinctions, it is not an absolute one.[18] An "as such" claim operates against a normative measure at a higher level of abstraction, intended to be of general and prospective application (such as legislation). The European Communities views on the so-called mandatory/discretionary distinction[19] do not suggest otherwise.

16. Furthermore, the European Communities agrees with the United States[20] that there is a distinction between a subsidy programme within the meaning of the *SCM Agreement* (which may be a measure at issue) and instances of a subsidy under such programme (each of which may also be a measure at issue). The former may be said to operate at a higher level of abstraction than the latter.

17. The European Communities also agrees with the United States that an actionable subsidies claim under Part III of the *SCM Agreement* refers to a "subsidy" within the meaning of paragraphs 1 and 2 of Article 1, which may be either a programme; or instances of the application of a programme; or both. These measures should not normally be conflated.[21]

18. The European Communities also agrees with the United States that a complaining Member must be especially diligent in setting out "as such" claims in panel requests and first written

[13] Brazil's First Written Submission, para. 333, second bullet point and footnote 510.

[14] *See* first bullet point.

[15] Brazil's First Written Submission, para. 333, second bullet point and footnote 510; Exhibit Bra-505.

[16] For example, in *Canada – Aircraft*, Canada changed the terms of the TPC programme (which was not an original measure at issue), and did not subsequently contest that it was a measure taken to comply. In *Australia – Automotive Leather II*, Australia changed the 1997 loan (originally found not to be an export subsidy) into a 1999 loan, which the compliance panel found to be within its terms of reference. In *EC – Bananas III (Article 21.5 – Ecuador)*, the EC changed its legislation, which was considered, in its entirety, to be within the compliance panel's terms of reference.

[17] US Rebuttal, paras. 22 to 24.

[18] For example, an original anti-dumping duty measure is often said to be attacked at the "as applied" level, although it is likely to be of general (residual duty per country) and prospective application.

[19] EC Third Party Written Submission, paras. 64 to 69; US Rebuttal, footnote 31.

[20] US Rebuttal, paras. 20 to 21.

[21] US Rebuttal, para. 25.

submissions; and that as long as either the existence or the precise content of the supposed measure is not demonstrated to a high threshold and with particular rigour, any such claims must be dismissed.[22]

19. The European Communities does see a difference between the type of programme, often fiscal, in which entitlement to payment is conditional only upon the fulfilment of certain essentially factual requirements, essentially in the hands of the recipient; and the type of programme in which application in any given instance still depends on considerations (sometimes referred to as "discretion") that are in the hands of the granting authority. In the latter case, the distinction between the programme and an instance of its application must be rigorously maintained.[23] In the former case the distinction may be less clear, and there may be a degree of nexus or interrelatedness or interdependence between the (for example, fiscal) programme and payments under it, such as might justify their treatment as indivisible for the purposes of a compliance panel.

20. The European Communities agrees with Brazil that, if a panel's adverse effects finding relates to a *bundle* of subsidies, the entire bundle will normally fall within the scope of a compliance panel. However, the European Communities agrees with the United States that this observation does not, *in itself*, resolve the question of whether the measures taken to comply relate only to the *payments*, or also the *programmes* themselves.

21. That said, the European Communities agrees with Brazil[24] that the fact that the United States implemented by withdrawing the Step 2 *programme* lends very considerable support to the view that there was at least a sufficient *nexus* between the Step 2 *payments* and the Step 2 *programme*. The Parties also agree that the original panel assessed a *bundle* of *payments* under the three different programmes – that is that the panel's adverse effects assessment assumed a *nexus* between the payments under the three different programmes. If there is sufficient *nexus* between payments and programme for one programme; and if there is sufficient *nexus* between all payments; this in turn suggests a sufficient *nexus* between all three programmes, such that the whole new bundle can and should be treated as indivisible for the purposes of this compliance panel.

22. The European Communities disagrees with the United States that the fact that something has not changed necessarily means that it is outside the scope of a compliance panel.[25] That depends on its relationship with what the Parties agree is within the scope of the compliance panel. And in any event Article 21.5 disputes may also relate to the question of whether or not a required measure taken to comply "exists".

23. Finally, and *significantly*, the European Communities observes that there is support in the case law for the view that claims of present serious prejudice and *threat* of serious prejudice are closely interrelated, such that a threat claim in an original panel may inevitably give rise to a claim of present serious prejudice in a compliance panel. It is not in dispute that Brazil's *threat* claims in the original panel were also made against the *programmes*.[26]

24. The European Communities interest in this matter being systemic, we do not venture a final view on whether or not the marketing loan programme and the counter-cyclical payment programme are or are not within the Panel's terms of reference; but we do respectfully invite the Panel to take the foregoing observations into consideration when reaching its findings on this point.

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[22] US Rebuttal, para. 41.
[23] As in the *Brazil – Aircraft* case, cited in US Rebuttal, paras. 51 to 52.
[24] Brazil's Submission Regarding the US Request for Preliminary Rulings, paras. 16 to 28.
[25] US Rebuttal, para. 18; paras. 53 to 61.
[26] Brazil's Submission Regarding the US Request for Preliminary Rulings, paras. 63 to 69.

C. COMPLIANCE IN PAST PERIODS

25. Paragraph 8.3(d) of the original panel report, as adopted by the DSB, contains a "recommendation or ruling" within the meaning of Article 21.5. Furthermore, one element of that "recommendation or ruling" was that the United States take appropriate steps to remove the adverse effects or withdraw the subsidy; and (by necessary implication) that should the United States fail to do so within six months from the date on which the DSB adopted the panel or Appellate Body Report, the consequences described in Article 7.9 of the *SCM Agreement* would result. In the opinion of the European Communities, it may reasonably be inferred from paragraph 8.3(d) of the original panel report and Articles 7.8 and 7.9 of the *SCM Agreement* that the United States was subject to a "recommendation or ruling" within the meaning of Article 21.5 that it take appropriate steps to remove the adverse effects or withdraw the subsidy at the latest within that six month period of time.

26. The Parties agree that the United States *omitted* to take a "measure taken to comply" during the period identified by Brazil. It follows that, during the period identified by Brazil, the United States did not comply with the "recommendations and rulings" of the DSB.

27. The United States argues that this situation is not within the scope of Article 21.5 because the Parties *agree* that no measure taken to comply existed during that period of time (and there is thus no "disagreement"); and that there could be no "disagreement" as to consistency, because there was no measure taken to comply.[27]

28. The European Communities disagrees. The United States overlooks the fact that any act or *omission* may be a measure for the purposes of dispute settlement.[28] It follows that, within the terms of Article 21.5 of the DSU, Brazil considers that the United States *omission* (in this context, the measure taken to comply within the meaning of Article 21.5) was inconsistent with a covered agreement, including Articles 7.8 and 7.9 of the *SCM Agreement*. This interpretation is consistent with, and indeed necessitated by, the view that, in some circumstances, inaction may be an appropriate method of implementation.[29]

29. The European Communities can find nothing additional in the terms of Article 21.5 that would limit its temporal application in the manner advocated by the United States. On the contrary, it seems to the European Communities that an integral part of a measure, apart from, for example, its material and territorial scope, is its temporal scope; and the European Communities does not see how this latter element could be artificially divorced from the whole. Apart from the fact that a non-compliance finding opens the way for retaliation, whether or not Brazil's request would ever be capable of having any practical utility is a different matter that this Panel does not need to address, being essentially a matter for Brazil, exercising its judgement in good faith.[30] In some instances, for example, it may be quite possible that such a finding could have implications for interested parties in a municipal law jurisdiction.

IV. ALLEGED EXPORT CONTINGENT SUBSIDIES

30. The European Communities does not comment on whether or not the alleged subsidies identified by Brazil are export contingent. However, the European Communities has four comments which relate rather to the question of whether or not the measures in question involve subsidies.

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[27] US Rebuttal, paras. 64 to 71.
[28] Appellate Body Report, *US - Corrosion-Resistant Steel*, para. 81.
[29] EC Third Party Written Submission, para. 41.
[30] Appellate Body Report, *US - Corrosion-Resistant Steel*, para. 89.

31. First, the European Communities agrees with the United States that Articles 14(a) to (c) of the *SCM Agreement* presume that the types of financial contribution there enumerated do not confer a benefit, unless the complaining party demonstrates otherwise.[31]

32. Second, the European Communities agrees with the United States that neither the status of bodies executing financial instruments, nor the terms on which they can borrow, determines whether or not such financial instruments confer a benefit.[32]

33. Third, the European Communities agrees with the United States that if estimated projected data indicate a negative net present value, that indicates profit, and there is accordingly no benefit and no subsidy.[33]

34. Fourth, the European Communities agrees with the United States that entities such as the International Finance Corporation (IFC), the Inter-American Development Bank (IDB) and the European Bank for Reconstruction and Development (EBRD) may provide commercial benchmarks that can be used for the purposes of demonstrating the absence of any benefit and thus the absence of subsidy.[34]

35. The European Communities respectfully invites the Panel to take these observations into consideration when reaching its findings on the alleged export contingent subsidies.

V. ACTIONABLE SUBSIDIES

36. The European Communities agrees with the United States that the data that the Panel must consider for the purposes of Brazil's claim of "present" serious prejudice would be the most recent relevant data reasonably available, including, where possible, data for the 2006 marketing year (which runs from 1 August 2006 to 31 July 2007).[35] Brazil agrees that the most recent data is relevant and should be referenced by the Panel.[36]

37. The European Communities further agrees with the United States that any consideration of data trends over time, in order not to be distorted, should be conducted in a meaningful way, that takes into account known exogenous events, or circumstances in which there were "entirely different market conditions", whether in the past or in the immediate future.[37]

38. The European Communities also agrees with the United States that where alleged subsidies are extinguished or extracted by owners not operating in the relevant markets, then there is no basis on which to find adverse effects, or for that matter a subsidy that continues to benefit the relevant company or product.[38]

39. The European Communities also agrees with the United States that, as long as the complaining party has failed to demonstrate that the effects of the subsidies are *significant*, including

[31] US Rebuttal, para. 79.
[32] US Rebuttal, paras. 80 and 104.
[33] US Rebuttal, paras. 84 and 87.
[34] US Rebuttal, para. 154.
[35] US First Written Submission, paras. 160 to 170; US Rebuttal, para. 182 and paras. 215 to 216: "… the period relevant for these claims is the immediate present, not a historical period (regardless of how close in time).".
[36] Brazil's Rebuttal, para. 25.
[37] US Rebuttal, para. 183.
[38] US First Written Submission, para. 215.

with specific reference to the *magnitude* of the subsidy, then the adverse effects claims should be dismissed.[39]

40. The European Communities respectfully invites the Panel to take these observations into consideration when reaching its findings on the actionable subsidies claims.

Mr. Chairman, distinguished Members of the Panel, the European Communities thanks you for your kind and patient attention.

[39] US First Written Submission, para. 236; US Rebuttal, para. 252.

ANNEX C-11

THIRD PARTY ORAL STATEMENT OF INDIA

28 February 2007

Mr. Chairman and Distinguished Members of the Panel,

1. India thanks you for having provided us an opportunity to present our views as a third party in this dispute on the implementation measures by the United States. As a major cotton producing country, with production dominated by low-income, resource poor, subsistence farmers, India has a major substantive interest in these proceedings. As a developing country India has a strong interest in a stable and competitive world market in cotton, unencumbered by trade and production distorting subsidies provided by a few countries. India shares the interests of Brazil and other like-minded parties to this dispute.

2. India fully agrees with Brazil, and those other third parties who have pointed out that the United States has failed to implement the recommendations and rulings of the Dispute Settlement Body in the original proceedings. We also agree with the contention that the United States continues to provide subsidies that either cause serious prejudice or threaten to cause serious prejudice, within the meaning of Articles 5 and 6 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement) and the relevant provisions of the GATT 1994.

3. India proposes to focus on the following two issues:

(i) The implementation with respect to Marketing Loan and Counter-Cyclical Payment (CCP) programmes by the United States; and

(ii) Export credit guarantee (ECG) programmes maintained by the Commodity Credit Corporation (CCC) of the United States.

4. As part of its implementation of the DSB recommendations on serious prejudice claims arising from the original proceedings, the United States claims to have repealed the Step 2 payment programme for upland cotton with effect from 1 August 2006, which was one of the programmes found by the original panel to be causing serious prejudice. The United States has argued that since Brazil had distinguished between claims against programmes *per se* and claims against specific *payments* under the programmes, the US Marketing Loan and Counter-Cyclical Payment programmes were not subject either to a finding of WTO inconsistency or any DSB recommendations. Accordingly, since these programmes have not changed in response to DSB recommendations and rulings or otherwise, the United States has requested this Panel to find that these measures are not within the scope of the present proceedings.

5. India recalls that, as upheld by the Appellate Body, the original panel found several mandatory price-contingent subsidy programmes of the United States, including the Marketing Loan and Counter-Cyclical Payment programmes, to be inconsistent with the obligations of the United States under Articles 5 and 6 of SCM Agreement. In view of the fact that the original panel considered the effect of these programmes separately and jointly, the United States cannot now argue that these programmes are outside the scope of this proceeding. India considers that the original panel examined carefully and separately the individual nature, operation, magnitude, and price-suppressing effect of these subsidies and found that the vast majority of the price suppression and adverse effects were caused by the marketing loan and counter-cyclical payment programmes, rather

than the Step 2 payments. Therefore, the withdrawal of the Step 2 payments for upland cotton cannot be said to have also removed the adverse effects of the Marketing Loan and CCP programmes.

6. Mr. Chairman, India also submits that the original panel clearly described the measures at issue as comprising the "legislative and regulatory provisions currently providing for the payment of measures", including Marketing Loan and Counter-Cyclical Payment programmes. The panel had clearly considered that its findings regarding "present" serious prejudice applied not just to payments, but also to the statutory and regulatory framework of the Farm Security and Rural Investment Act, 2002 and its implementing regulations. Contrary to the arguments put forward by the United States, the U.S. obligations at the implementation period were not circumscribed to "payments" made in a period in the past. Therefore, an examination of the conformity of the legislative and regulatory provisions, under which the mandatory, price-contingent Marketing Loan and CCPs are made, with the rulings and recommendations of the original panel and Appellate Body, falls within the terms of reference of this Panel. An interpretation that would endorse the U.S. arguments on this issue would, in practice, render the whole Part III of the SCM Agreement ineffective. This is not an interpretation supported by the principles and rules of treaty interpretation used in the WTO, and would be of even more concern in light of the specificity of the remedies provided for in that Agreement.

7. Mr. Chairman, with respect to the three export credit guarantee (ECG) programmes maintained by the Commodity Credit Corporation (CCC) of the United States – GSM 102, GSM 103 and SCGP – the Dispute Settlement Body recommended that the United States withdraw the subsidy and otherwise bring itself into compliance with its obligations by the implementation deadline of 1 July 2005.

8. In India's view, in the absence of GSM 102 fees that take full account of all the risks the CCC bears in a transaction, the measures taken by the United States to comply with the DSB's ECG related recommendations are not consistent with the obligations of the United States under the Agreement on Agriculture and the SCM Agreement. In its submission, Brazil has demonstrated clearly that under Article 1.1 and 3.1(a) of the SCM Agreement, GSM 102 ECGs are financial contributions that confer benefits, and that the subsidies are contingent in law on export performance. India also agrees with Chad, who in their written submission has shown why, as a practical matter, only developed country governments can effectively provide ECGs to promote their exports. India also believes that purchases of goods backed by US ECGs benefit from the sovereign guarantee, thereby giving a competitive advantage to US exporters. Therefore, Mr Chairman, India is of the view that the GSM 102 programmes are still not in compliance with the export subsidy disciplines specified in Articles 1.1 and 3.1(a) of the SCM Agreement and the Agreement on Agriculture.

Thank you.

ANNEX C-12

THIRD PARTY ORAL STATEMENT OF JAPAN

28 February 2007

I. Introduction

1. Mr. Chairman and Members of the Panel, we are pleased to have this opportunity to appear before you today to present the views of Japan as a third party in this case. Japan is participating as a third party because of its systemic interest in the proper functioning of the Agreement on Subsidies and Countervailing Measures ("ASCM") and the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), in particular, the proper role of Article 21.5 compliance panels. This Panel has an important opportunity to clarify that role. We would like to briefly address, in light of the Written Submissions of Brazil and the United States ("U.S."), three issues concerning the role of Article 21.5 compliance panels under the DSU and one issue regarding the proper interpretation of the ASCM:

- Whether the use by the U.S. of the General Sales Manager ("GSM") 102 program to support exports of pig and poultry meat is within the scope of the Panel;

- Whether the Marketing Loan Program ("MLP") and the Counter-Cyclical Payment Program ("CCP") are part of the U.S. "measure taken to comply" and, therefore, within the scope of the Panel;

- Whether the Panel has the authority to make findings with respect to the U.S. non-compliance between 21 September 2005 and 31 July 2006; and

- The proper standard for assessing "threat of serious prejudice" in the ASCM.

II. The GSM 102 Program for Pig and Poultry Meat Is Within the Scope of the Panel

2. In the original proceedings, the Appellate Body reversed the original panel's finding that Brazil had failed to demonstrate that the U. S. had applied GSM 102 in a manner that circumvented export subsidy commitments with respect to pig and poultry meat, but concluded that there were insufficient uncontested facts in the record to enable it to complete the legal analysis.[1] Based on this fact, the U.S. asserts that Brazil's claim is outside the scope of this Panel. In Japan's view, this assertion by the U.S. is not an appropriate interpretation of Article 21.5 of the DSU.

3. The Appellate Body's inability to complete the analysis concerning a finding it has reversed is similar to an original panel's exercise of judicial economy; both situations mean that there is no "final resolution" with respect to the claim in question, and no reason to preclude its resolution in an Article 21.5 proceeding.[2] Thus, Japan submits that the recent report of the Article 21.5 compliance panel in *U.S. – OCTG Sunset Reviews* is dispositive:

> The fact that a panel, in an original dispute settlement proceeding, did not make findings regarding certain issues relating to the investigating authorities' determination that were raised and argued before the panel, can not preclude a compliance panel, in its assessment under

[1] *United States – Subsidies on Upland Cotton*, WT/DS267/AB (3 March 2005), paras. 689-694.
[2] *See* Submission of Brazil to the Panel Regarding U.S. Requests for Preliminary Ruling, note 14.

> Article 21.5 of the DSU of the measures taken to comply with the recommendations and rulings, from reviewing those aspects which have been incorporated by the authorities in the measure taken to comply.[3]

4. Japan respectfully submits that, as indicated by the report of the Article 21.5 compliance panel in *U.S. – OCTG Sunset Reviews*, this Panel has the authority to identify and assess the new U.S. measures taken to comply with the recommendations and rulings of the DSB, *i.e.*, the MLP, the CCP, and the GSM 102, GSM 103 and Supplier Credit Guarantee Programs, including the GSM 102 Program for Pig and Poultry Meat.

III. MLP and CCP Payments Are Part of the U.S. Measure Taken to Comply

5. For the reasons presented by Japan in its Third Party Submission, the assertion by the U.S. that the panel lacks the authority to address Brazil's arguments regarding the U.S. MLP and CCP payments is flawed.[4]

6. Japan agrees with Brazil that the question before the compliance Panel is whether the new basket of U.S. price-contingent measures (MLP and CCP), which constitutes the "measures taken to comply", is "consistent with the covered agreements". This basket includes payments under the programs–actions by the U.S. with an impact on the market for cotton. The focus of the Panel, therefore, should be on the payments made under the programs, rather than the programs as such.[5] To comply with WTO obligations, the U.S. should have taken steps to ensure that the adverse effects no longer exist.[6]

7. Japan thus respectfully submits that the Panel must reject this argument by the U.S.

IV. The Panel Has the Authority to Make Findings With Respect To the U.S. Non-Compliance between 21 September 2005 and 31 July 2006

8. The U.S. submits that there is no "disagreement" between the U.S. and Brazil as to the existence of measures taken to comply with the recommendations and rulings of the DSB as stipulated in Article 21.5 of the DSU.[7] The non-existence of measures taken to comply may not be subject to review by a compliance panel if there is no such "disagreement". However, in this case, a disagreement does exist between Brazil and the U.S.–one party (Brazil) is of the opinion that there is a disagreement. The U.S. cannot simply make the disagreement go away by stating that Brazil agrees with the U.S. Alternatively, one may view the U.S. position as a concession that, indeed, it failed to comply because it took no actions during the period in question. In any case, the U.S. argument must be rejected as an attempt to remove from Article 21.5 review precisely the most egregious violations–cases in which a Member does nothing whatsoever to comply.

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[3] *United States—Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina*, WT/DS268/RW (30 November 2006), para. 7.92.

[4] Third Party Submission of Japan, paras. 18-21.

[5] Third Party Submission of Australia, para. 15.

[6] The Third Parties to this dispute are nearly unanimous in taking this view. *See* Third Party Submission of Australia, para. 25-31; Third Party Submission of Canada, para. 14; Third Party Submission of Chad, paras. 35-46; Third Party Submission of China, paras. 9-16; Third Party Submission of New Zealand 4.11.

[7] First Submission of the U.S., paras. 49-56.

9. As Australia notes, a failure to address this claim by Brazil would diminish Brazil's rights under Article 22 of the DSU.[8] Thus, the disagreement on the non-existence of the compliance measures is properly before this Panel.

V. The Panel Should Carefully Consider Any Proposed Standards for Threat of Serious Prejudice

10. Japan is of the view that the most important issue of general interest raised in this dispute is the appropriate standard for establishing threat of serious prejudice under Part III of the ASCM.[9]

11. A threat of serious prejudice standard should contain two elements – a legal standard and an evidentiary requirement. The legal standard should not be based on the standard in Part V of the ASCM. Part III issues are devoid of concerns relating to limiting the discretion of national authorities to prevent misuse thereof in the conduct of domestic CVD investigations that apply to Part V. Therefore, Japan does not agree with the assertion by the U.S. that Article 15.7 of the ASCM and Article 4.1(b) of the Agreement of Safeguards provide important contextual guidance in interpreting "threat" of serious prejudice under Part III of the ASCM.[10]

12. Brazil proposes that the Panel find that a "threat of serious prejudice" exists where there is a "'significant likelihood' of serious prejudice in the future."[11] However, Brazil's proposed standard offers little concrete guidance.

13. The legal standard must be tied to an evidentiary requirement. An explicit evidentiary requirement such as that set forth in the first sentence of Article 15.7 of the ASCM[12] is a crucial component of any "threat" standard. It is necessary to tie to real world facts what otherwise is an amorphous concept.

14. Japan asks the Panel to consider these views when examining the issue of the proper standard for threat of serious prejudice.

VI. Conclusion

15. Japan would like to thank the Panel for this opportunity to raise these issues concerning the proper functioning, as required by the DSU, of the compliance phase of the dispute settlement process.

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[8] Third Party Submission of Australia, para. 21.

[9] *See* ASCM, Article 5(c) and note 13.

[10] Rebuttal Submission of the U.S., para. 411.

[11] First Submission of Brazil, para. 259.

[12] *See also* Agreement on Safeguards, Article 4.1(b) ("A determination of the existence of a threat of serious injury shall be based on facts and not merely on allegation, conjecture or remote possibility"); AD Agreement, Article 3.7 ("A determination of a threat of material injury shall be based on facts and not merely on allegation, conjecture or remote possibility").

ANNEX C-13

THIRD PARTY ORAL STATEMENT OF NEW ZEALAND

28 February 2007

Mr Chairman, Members of the Panel,

Introduction

1. New Zealand has a systemic interest in this dispute and welcomes the opportunity to participate in this oral hearing. We wish to make brief comments on three areas, recognising that our views have been presented to you already in our third party submission. Firstly we will comment on why we believe the marketing loan payments and counter-cyclical payments are indeed within the scope of this Article 21.5 proceeding; secondly we will make a brief comment on the burden of proof in a case such as this; and finally we will explain why we believe the marketing loan payments and counter-cyclical payments continue to cause adverse effects.

The scope of this 21.5 proceeding

2. In our view the payments made under the marketing loan payments programme and the counter-cyclical payments programme are clearly within the scope of this proceeding. The panel was clear in paragraph 8.1(g)(i) of its report that its finding was about the "effect of the mandatory price-contingent United States subsidy measures." A reference to payments does not alter that finding. Payments are not mandatory subsidy measures; they are simply the means by which the subsidy measures are implemented. The distinction made by the United States between payments and programmes would undermine the disciplines on actionable subsidies in the SCM Agreement.

3. Of particular importance is the need to give effect to the remedy provided for in Article 7.8 of the SCM Agreement, as referred to by the original Panel in this dispute. This is the first time the relationship between Article 21.5 of the DSU and Article 7.8 of the SCM Agreement has come before a compliance proceeding. Given that the marketing loan and counter-cyclical payments programmes have not been withdrawn, the United States cannot now avoid its obligation under Article 7.8 of the SCM Agreement to remove the adverse effects of those subsidy programmes by claiming that they are not measures taken to comply within the meaning of Article 21.5 of the DSU. In New Zealand's view, if the measures are not withdrawn Article 7.8 of the SCM Agreement then requires the Panel to determine whether steps have been taken to remove the adverse effects found to exist by the original Panel. It must then determine whether any steps that have been taken are "appropriate", that is whether they are measures that are capable of removing the adverse effects. Article 21.5 of the DSU cannot be invoked as a barrier to such an analysis.

Marketing Loan Payments and Counter-Cyclical Payments continue to cause significant price suppression and increase the world market share

Burden of proof

4. As in our submission, we wish to make a brief comment regarding the burden of proof in a case such as this. The DSB recommendations and rulings of 21 March 2005 covered three programmes: the step 2 payments programme; the marketing loan payments programme; and the counter-cyclical payments programme. Having chosen to remove only one of those programmes the United States now claims that Brazil has the burden of showing that the remaining

two programmes cause serious prejudice. The United States conveniently ignores the fact that the original Panel had already evaluated the evidence and made a finding that all three programmes cause adverse effects. A Member should not have the burden of proving something that has already been decided by the original panel. In this case that would deprive the actionable subsidies provisions of the SCM Agreement of their proper effect.

5. Since an implementing Member has the option of either withdrawing the subsidising measure or removing the adverse effects under Article 7.8 of the SCM Agreement, an implementing Member that fails to withdraw the measure in question then should have the burden of showing that it has removed the adverse effects. Thus, in the present case proof by Brazil that the measures found by the original panel to cause adverse effects have not been withdrawn should establish a prima facie case that implementation has not occurred. In New Zealand's view, the burden would then be on the United States to prove that the adverse effects caused by those subsidising measures have been removed.

The adverse effects from the Marketing Loan Programme and the Counter-Cyclical Programme remain

6. We agree with Brazil that the removal of the Step-2 programme had a relatively modest impact. A comparison of the amounts paid under the various programmes shows significant differences. Step 2 payments are small compared to marketing loan and counter-cyclical payments. In the most recent year, 2005, for example, the Step 2 payments were US$350 million. In the same year, the marketing loan and counter-cyclical programme payments amounted to US$2,170 million. The US cannot ignore the much larger volume of subsidisation under the two programmes that have not been withdrawn or modified.

7. Also, it is possible – and likely – that the counter-cyclical payments could increase to compensate for the removal of the Step 2 programme. The United States argues against this line of reasoning given that there was no increase in counter-cyclical payments in the current year. What the United States fails to make clear is that those payments are already at their maximum rate. If that were not the case there could indeed be a compensatory effect for the removal of the Step 2 programmes.

8. The United States attempts to counter Brazil's arguments about the trade-distorting effects of counter-cyclical payments by blurring the line between counter-cyclical payments and decoupled payments. But, counter-cyclical payments are not real decoupled payments.

9. Real decoupled payments are green box measures and cannot be linked to the type or volume of production or be related to or based on prices. Counter-cyclical payments, by contrast, are clearly and explicitly linked to prices. The fact that in many years such payments are likely to be paid out at the maximum rate does not change the fact that they are linked to prices. The question is, what would farmers do differently if there were no counter-cyclical payments and farmers were, essentially, "guaranteed" 13.73 cents per pound less for their cotton.

10. Indeed, the United States fails to accurately explain the role of expectations in the market place. While it is possible that removal of the Step-2 programme will decrease the marketing loan payments, this argument ignores the fact that these programmes are distorting whether or not payments are made under them. Producers know that the loan rate is there to support them and that there is a target price they will receive either from the market or the government.

11. In fact, the proposition that marketing loan payments are distorting is almost self-evident. Marketing loan payments are amber box measures, the category in which are included the non-prohibited measures with the most trade distorting effect on production and trade. Producer

expectations are generated because of applied administrative prices under a subsidisation programme – because of a guaranteed price, regardless of what happens in the market place – not because of financial transfers in any one year. Producers are aware that they are insulated from the market place by government support and it is this guarantee of insulation that affects producer decision making.

12. The United States tries to convince you that producers respond to market signals, and that the marketing loan programme and counter-cyclical programme do not insulate producers from the market. But, in the absence of the marketing loan and counter-cyclical programmes – programmes that guarantee certain prices to producers of cotton in the US – would the United States market share of cotton be at current levels? The link that is necessary to examine is that between domestic, guaranteed prices and United States production. And that is the source of the problem.

13. The United States contests the Brazilian argument that absent the payments farmers would exit cotton production. This ignores the evidence. Over some years over half of the revenues received by United States cotton farmers has come from subsidisation. The idea that if these subsidies were not there, producers who have been deprived of half of their income would carry on planting cotton is little short of absurd.

14. The United States also claims that the econometric modelling provided by Brazil is flawed, but the arguments of the United States are either an attempt to reargue what was litigated before the original panel and the Appellate Body and lost, or are inconsequential.

15. The United States itself demonstrates that if the marketing loan and counter-cyclical payments programmes were eliminated there would be a reduction in United States cotton exports of up to 25 per cent in 2002-2005 and 17 per cent in 2006-2008. That is a very clear measure of what United States world market share would be in the absence of the marketing loan and counter-cyclical payments programmes.

Conclusion

16. In conclusion, in New Zealand's view, Brazil has demonstrated that the United States has failed to either withdraw the marketing loan and counter-cyclical payments programmes or to remove the adverse effects of those programmes as required by Article 7.8 of the SCM Agreement. Accordingly, the United States has failed to comply with the recommendations and rulings of the DSB.

ANNEX C-14

THIRD PARTY ORAL STATEMENT OF THAILAND

28 February 2007

1. Mr. Chairman and Members of the Panel: Thailand appreciates the opportunity to participate in this proceeding and to present its views to the Panel today.

2. Thailand reserved its right to participate as a third party in this proceeding under Article 10.2 of the *Dispute Settlement Understanding* due to our interest as one of the top global exporters of rice. As demonstrated by Brazil, rice is one of the products affected by the Export Credit Guarantees (ECGs) maintained by the United States Commodity Credit Corporation (CCC) under the GSM 102, GSM 103 and SCGP programs. In fact, according to Brazil's first submission, almost half of the USD 8.5 billion of ECGs outstanding as of 1 July 2005 involved rice and other products.[1]

3. Mr. Chairman, a fair playing field for rice exports is essential to Thailand's development. Not only are Thailand's climate and geography particularly suited to rice cultivation, the farming and production of rice affects over 4 million households located mostly in Thailand's rural areas. We therefore generally share and support Brazil's concerns regarding the United States' implementation in this dispute and its continued provision of ECGs subsequent to the withdrawal date of 1 July 2005 recommended by the Dispute Settlement Body.

4. In particular we find troubling the continued maintenance of GSM 102 ECGs by the United States. Although the United States claims that it has amended the GSM 102 program and that ECGs provided thereunder are now WTO-consistent, Thailand views that the ECGs are still provided on non-commercial terms such as the mandatory one-percent fee cap and failure to take into account all relevant risks faced by the CCC.[2]

5. As Brazil has already submitted comprehensive analyses on the aforementioned aspects of GSM 102 in its submissions, as well as the resultant circumvention by the United States of its export subsidy commitments[3], Thailand will not repeat those arguments here. We would only emphasize Brazil's demonstration that GSM 102 bridges the financial gap between United States exporters and foreign buyers to make the export sale possible. Without such assistance from the United States government, agricultural exports under GSM 102 would not occur.[4]

6. While a large developed country Member such as the United States can afford to finance its agricultural exports through programs such as GSM 102, Thailand empathizes with the concern expressed by Chad in its written submission that developing country and LDC Members "face permanent structural disadvantages compared to developed country Members in providing export credit,"[5] even if such schemes were consistent with WTO disciplines. In light of this concern, and of the persuasive arguments and evidence submitted by Brazil, we urge the Panel to make the relevant findings and recommendations requested by Brazil in its First Submission. Thank you.

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[1] First Written Submission of Brazil, 17 November 2006, paras. 344 and 345.
[2] *Ibid.* paras. 419-421and paras. 445-446.
[3] *Ibid.* paras. 448-452.
[4] *Ibid.* paras. 4356-357.
[5] Written Submission of Chad, para. 53.